



European Commission
Employment, Social Affairs and Equal Opportunities
DG – Directorate F – Unit F3
Project Ref. VT/2008/096

Final Report:

The impacts of private equity investors, hedge funds and sovereign wealth funds on industrial restructuring in Europe as illustrated by case studies

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Manuscript completed in August 2009

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The information contained in this publication does not necessarily reflect the position or opinion of the European Commission.

This publication is supported under the European Community Programme for Employment and Social Solidarity – PROGRESS (2007-2013).

This programme is managed by the Directorate-General for Employment, social affairs and equal opportunities of the European Commission. It was established to financially support the implementation of the objectives of the European Union in the employment and social affairs area, as set out in the Social Agenda, and thereby contribute to the achievement of the Lisbon Strategy goals in these fields.

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Executive Summary

1. The growth of the volume of assets under management by hedge funds (HFs), private equity funds (PEFs), and sovereign wealth funds (SWFs) is one of the most striking phenomenon in the international financial system in the last 20 years. It is a common belief that the direct investments by these funds in companies influence corporate development: In particular hedge funds and private equity funds are perceived as investors with a significant impact on business decisions and restructuring at company level.
2. Against this background this report focuses on two major research issues: First, the influence of these investment funds on companies, their strategies and corporate development and secondly, the impact of this influence on industrial change and the functioning of the "real economy" throughout Europe, e.g. in terms of employment development, working conditions and industrial relations.
3. These research questions are addressed on the basis of seven case studies illustrating investment by SWFs, hedge funds and private equity. We are aware that such a small number of seven case studies can only illustrate examples of specific company contexts and are not necessarily representative for the whole population of investments. Therefore the findings and examples in this study have to be seen in the context of other research work on strategies and behaviour of capital funds as addressed for example by European institutions, key actors and the research community. Our review illustrates the controversial character of the debate on both macro- and micro-level effects of private and state-owned capital funds on industrial change and restructuring in Europe.
4. The researcher is always confronted with the methodological problem which can be described as the "*question of the counterfactual*". Information and data on industrial change in companies with alternative investments therefore needs to be compared with data on other similar companies which have not changed ownership. In order to address this methodological problem we have included in each case study report a section which contrasts/compares the individual case with the overall development and structural change in the respective sector and national context.
5. It should be stressed that a major barrier for any assessment of the impact of the three types of investment funds on industrial restructuring in Europe is the lack of available data and information. As our analysis shows, no single data base gives an estimate of how many European companies the different types of funds are invested in or which share of ownership investment funds hold. However, the overview of the relative size of funds under management illustrates the growing influence of these funds.
6. It is not possible to give exact numbers in how many companies the different types of funds are invested. For PE we can estimate from the existing data that more than 10,000 companies of all sizes in Europe are affected by this type of fund investment. For hedge funds no estimate can be made, but the typical hedge fund investment is in a listed company. SWF are directly invested in a much smaller number of companies. The typical SWF investment is in larger companies, either as a majority investor or as an important minority stakeholder.
7. The UK is by far the most significant of the six countries analysed in the study for private equity and hedge funds (in both cases as both a headquarters for fund management and a location for investment) and for sovereign wealth funds as an investment location. Our study also reveals that SWF positions in UK-listed companies were considerably larger and more concentrated than in other European countries.

8. Our fund-specific analysis shows major differences in the respective business models and investment strategies of the three types of funds. This variety is further increased when taking into account the individual funds which play the most relevant role in the companies addressed in our case study analyses.
9. With regard to the impact of the three types of funds on industrial restructuring at company level, it is important to stress that the concrete outcomes are largely driven by the respective business models as well as fund-specific strategies. There are important differences with regard to aspects such as main investment focus and the investment horizon/duration. Beside these general differences *between* the three types of funds also differences *within* each group matters with regard to the role of these funds in different stages and situations of business development. Furthermore, it is important to differentiate between two different styles of investment behavior – *passive* and *activist* – which also is not necessarily determined by the fund type.
10. With regard to concrete impacts of capital funds on industrial change and restructuring as illustrated by individual cases, the main focus of the analysis is on the impact at the company level. For this report three broad dimensions for measuring impact were defined: company performance, changes in employment and labour relations and other factors like effects of transmission to the whole sector and others.
11. The Italian case of *Marazzi* illustrates a positive impact of private equity investment practice on growth and expansion, at least until the global financial and economic crisis of 2008.
12. The Spanish case of *DinoSol* illustrates effects of a major PE investment fund on company restructuring and industrial change. The case illustrates how a PE controlled company works, setting financial parameters, but then devolving most aspects of management to local managers, many of whom are incumbent managers. This is particularly the case with industrial relations issues.
13. In Poland, which has the lowest absolute level of PE activity among the six countries studied, the case of *Zelmer* illustrates the practice and corporate influence of PE investment. Originally a state-owned company, the case shows the influence of private equity funds on structural change and restructuring.
14. Two cases in our sample are located in Germany: *KUKA* is an example of a continuous adaption process to a fast changing economy and the impact of HF investment on this process. The case illustrates an example of activist shareholder practice which resulted in a comparatively rapid restructuring process. A contrasting example of hedge fund investment is provided by the case of *Schefenacker*, which is an interesting case because it includes an attempt to achieve industrial growth in a highly competitive world market by buying other companies. Schefenacker also is an example for a very creative and successful attempt of employees and the local trade union to save as many jobs and parts of the old company after the failure of management and its strategy.
15. The case of the French company *Cegelec* illustrates the practice and impact of both PE investments as well as the effects of a major global SWF on company development with two leveraged buy-outs between 2001 and 2008. The case illustrates in first phase a PE business logic which is oriented towards a short term sale and in the second phase an investment by a SWF.
16. In the UK, the case of *P&O* was chosen as an example of SWF investment, following a period of substantial restructuring and acquisition by a major SWF, which gave it a stronger position in Europe and the rest of the world.

17. Though there are well-known limitations of the case study approach, the seven case studies analysed allow for some general conclusions with regard to the impact of the three types of funds on industrial restructuring at company level.
18. The PE cases illustrate major aspects and two basic orientations of the PE business model: First, a typical investment linked to a growth strategy (as in the cases of Marrazzi and also Zelmer). In these cases PE offers an opportunity to realize expansion into new markets, which is risky and not feasible without risk capital. If the strategy works out and economic performance is sufficiently high all partners involved end up with high returns on their investment. Secondly, and following another business model, PE may invest in an undervalued company with a good growth perspective, free cash flow and assets that can be capitalized for financial reengineering strategies. Cases like Cegelec and Dinosol are in many ways typical for this type of PE activities.
19. In contrast to PE the evaluation of the HF approach and its impact on industrial change is more complex, partly resulting from a lack of transparency and partly as a consequence of the free style investment approach of HF. Our case studies for HF investments also show two different investments: Strong short-term orientation following an active investor (KUKA) and a high risk debt financing strategy after the strategy of the former owner had failed (Schefenacker).
20. The two SWF investments analysed by case study examples show on the one hand the expected long term orientation of the investors and also the possible (but so far not proven) linkage strategy to national development goals of the investor. However, this does not cover the situation where SWFs take smaller ownership stakes in listed companies.
21. Given the large differences between the cases any assessment of the impact on industrial restructuring and economic success of the companies has to be elaborated in a differentiated and cautious way. In fact, it is difficult to draw firm conclusions since there are no accepted criteria for measuring impact, success or failure. In general the case studies show the catalytic effect active investors can have on industrial change. In any case the effects have to be analysed in both a short term and a long term perspective.
22. The different circumstances in each case make it difficult to come to any conclusions regarding the impact on employment. If the investment by PE, HF or SWF is successful and there is long term growth of the company one would expect a positive impact on employment figures. However, at least in some cases of investments by PE and HF there exist some strong indications that the withdrawal of financial resources and the concentration on core business lead to job losses in company sites which are closed down or sold.
23. Regarding wage developments and working conditions, in the long term perspective the case studies provide no indications for a worsening of the situation after the entrance of an alternative investor. The cases show that this very much depends on the economic situation of the company.
24. A quite striking feature of all cases analysed is the adaptation of the investors to national rules that relate to all forms of social dialogue. In most cases the investors are not visible to the employee representatives and local management is used to implement changes and new strategies.
25. To sum up, the seven cases lead to a mixed picture of the effects on industrial restructuring at company level: In some cases investors as HF or PE have a positive impact on company performance and restructuring processes – a fact which is frequently repeated by the PE business community. In the case of active investors, a conclusion of the cases analysed is that this type of investment accelerates re-

structuring and structural change. As far as the impacts of SWF are concerned some other positive factors could be important. One proposition is that SWF represents a new form of long term orientated "patient" capital which gives the companies additional resources and longer times periods for investments. Additionally, our case study analysis shows that new markets can be opened up with the support of SWF capital.

26. On the other hand our case studies also present some insights on the negative impact of these investors: For PE investments the most obvious negative impacts on company development and industrial restructuring are directly linked to the economic goals of these investment vehicles, i.e. buying companies, restructuring them and selling them for a higher price. Between purchase and sale there is a phase of freeing financial resources. This can be done by financial re-engineering strategies (e.g. financing part of the purchase price as a loan to the company, capitalizing assets and withdrawing financial resources from the companies) resulting in undercapitalized companies which run into severe economic problems as soon as the macro economic environment deteriorates. For HF the negative impact factors are linked to the short term nature of their investments and their lack of transparency. Though this is not proven by the cases analysed in our study, a possible risk linked to SWF is seen in the linkage to political goals of the states behind the funds. In fact, the practical knowledge and the transparency of these funds is so low that we can only guess what the positive or negative impact are.
27. This lack of transparency is clearly an important issue of concern: There is a real need for further research on this matter and an intensive political debate which should focus on the issue of transparency on the investment of all three types of funds.

PART I:

BACKGROUND AND CONTEXT

1 Introduction and overview on this report

The growth of the volume of assets under management by hedge funds (HFs), private equity funds (PEFs), and sovereign wealth funds (SWFs) is one of the most striking phenomenon on the international financial market in the last 20 years. This growth is linked with the fundamental changes in industry and financial markets in the context of globalisation. As a consequence also the number of investments by PE, HF and SWF in companies has increased dramatically.

It is a common belief that these direct investments in companies by PE, HF and SWF influence corporate development. Especially hedge funds and private equity funds are perceived as active investors which have a large impact on business decisions at company level. Therefore, a crucial question is what consequences the growing role of private equity, hedge funds and also sovereign wealth funds has on industrial development. The main research questions of this report are:

- *What influences do these investment funds have on companies, their strategies and development?*
- *What impact has this influence on industrial change and the functioning of the "real economy" throughout Europe, e.g. in terms of employment development, working conditions and industrial relations?*

Our report is based on a selection of seven company-orientated case studies in six European countries. We have tried to choose these case studies in a way that two or three cases for the investment strategy and behaviour of each fund category are described. We analyse two companies with an investment by SWF, two cases with an investment by hedge funds and three cases with an investment by private equity.

However, given the large number of European companies in which PE, HF and SWF are currently invested in such a small number of case studies (seven) can only illustrate investment strategies and behaviour of HF, PE and SWF. We know that the selection of cases is not representative of the whole population of investments. The best one can say is that our case studies describe a fair balance of relevant business cases and strategies of the different financial actors.

Therefore the findings and examples in this study have to be seen in the context of other research work on strategies and behaviour of capital funds. Several European institutions and key actors such as the European Commission¹, the European Parliament as well as social partner organisations and business organisations have addressed these

¹ See "EU Commission Open Hearing on Hedge Funds and Private Equity", February 26th & 27th 2009. http://ec.europa.eu/internal_market/investment/docs/conference/summary_en.pdf

questions, leading to an ongoing debate on the nature, functioning and effects of capital funds.

The debate is very controversial on both macro- and micro-level effects of private and state-owned capital funds on industrial change and restructuring in Europe. While several surveys and studies highlight the overall long-run positive effects of these funds on employment creation, innovation and other aspects of business development in Europe², other surveys report negative effects both at the level of micro-economic restructuring (i.e. reducing wages, R&D investments and the long term innovation capacity in favour of short term profits) as well as on the sustainability of financial markets in Europe.³

In a study for the Consultative Commission on Industrial Change at the European Economic and Social Committee we carried out in parallel to the case study research presented here we analysed the existing data on the magnitude of PE, HF and SWF investments in Europe and reviewed the fast growing research literature with respect to an impact assessment of these funds. Additionally we have compiled a catalogue of possible factors through which investment funds impact industrial change at a micro and macro level (i.e. on the level of the company and on the level of national and international economic structures).⁴

In the following chapters of the first part of this report we present an overview on the role and financial impact of investments by PE, HF and SWF in Europe aiming at presenting an indication of how relevant the activities of these funds are for industrial change. The first part also includes general remarks and information on the respective functioning and business models of the three types of funds as well as methodological considerations on how to analyse and assess different dimensions and impacts on industrial change at the company level. The intention here also is to put the case studies in a broader framework and to avoid misinterpretation and overgeneralization of impressions gained from events in individual companies.

The second and main part of this report presents the seven case studies carried out by national co-authors in Italy, Spain, Poland, Germany, France and the United Kingdom. Each case study report follows a similar rationale, i.e. presenting some general context information and figures on the role of the three types of funds on the respective national financial markets and then describing and analysing the individual company case and restructuring processes in detail.

In the final part of this report we draw some general conclusion and position our case studies in the context of other research and present conclusions of our research work.

Our report includes two annexes: First, overview tables and figures on the role and development of PE, HF and SWF in the six countries addressed in our research and secondly, a synoptical (and not exhaustive) overview of other case study findings in order to compare and contrast our findings with others research.

² See for example: Achleitner, Ann-Kristin and Klöckner, Oliver (2005): "Employment Contribution of Private Equity and Venture Capital in Europe", Centre for Entrepreneurial and Financial Studies (CEFS) on behalf of the European Private Equity and Venture Capital Association (EVCA).

³ See for example: Van den Burg, Ieke and Rasmusen, Poul Nyrup (2007): "Hedge Funds and Private Equity – A Critical Analysis", Socialist Group in the European Parliament.

⁴ See Voss, Eckhard et al. Data collection study on the impact of private equity, hedge and sovereign funds on industrial change in Europe, Hamburg, June 2009.

2 The dimension of investments of private equity, hedge funds and sovereign wealth funds in Europe

Before analysing the impact and the consequences of the activities of different kinds of funds at company level it would be helpful to have an indication how relevant these investments by funds are for companies in Europe. Unfortunately there is no common data base to answer this question. No single data base can give an estimate of how many European companies the different types of funds are invested or which share of ownership investment funds hold.

An overview of the relative size of funds under management of PE, HF and SWF shows the growing influence of these funds. Compared to private wealth, pension funds and other forms of assets, the overall volumes in PE, HF and SWF are however still relatively small and comprise only a small portion of the financial resources invested in firms. However, they are significant enough to influence a large number of companies.

While the relative size of HF, PE and SWF is growing at a global level the economic influence of these funds is increased by the use of debt leverage of 2-3 times in relation to the capital under management. Additionally the activities of most funds are concentrated on a limited number of markets, mainly in the US and Europe. The following table shows the relative importance of different investor types, in terms of assets under management, at a global level.

Global assets under management

Rank	Fund type	\$ billions	Figures as of
1	Pension funds	\$ 28,228	2007
2	Mutual funds	\$ 26,200	2007
3	Insurance companies	\$ 18,836	2007
4	Real estate	\$ 10,000	2006
5	Foreign exchange reserves	\$ 7,341	February 2008
6	Sovereign wealth funds	\$ 3,300	2007
7	Hedge funds	\$ 2,300	2007
8	Private equity funds	\$ 2,000	2007
9	REITs	\$ 764	2007

Note: Around one third of private wealth is incorporated in conventional investment management (Pension funds, Mutual funds and Insurance assets). Source: International Financial Services London.

2.1 Private Equity

A short definition of Private equity describes it as an equity investment in a private company that is not listed in a stock exchange. Private Equity is seen as an own asset class including either an investment of capital into an operating company or the acquisition of an operating company. Capital for private equity is raised primarily from institutional investors.

Data reports suggest that Europe accounts for somewhat less than one third of global PE activity. Overall global PE investment for 2007 was estimated at \$ 297 billion, with a breakdown by country indicating that Europe accounted for about \$ 85 billion.⁵

PE is concentrated in certain types of activities, such as mergers and acquisitions (M&A), accounting for up to 28% of M&A quarterly deal volume in Europe and for an even greater proportion of buyout activity. Per Stroemberg's study for the Davos 2008

⁵ PriceWaterhouseCooper Private Equity Report 2008, p. 41-42.

PE report shows that, historically, PE has financed 80 % of buyout deals by number and 92 % by financial value.⁶

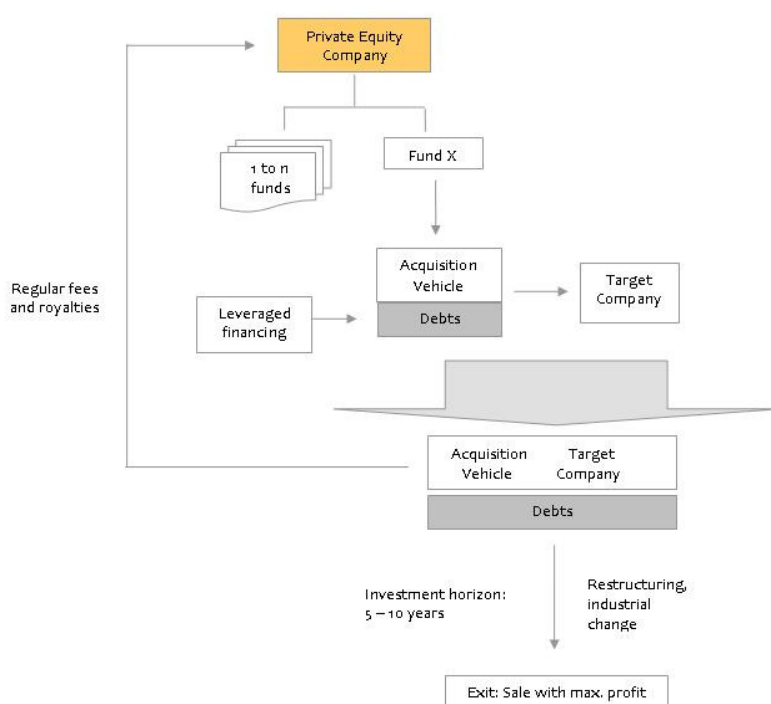
EU M&A Activity (Overall and PE-Driven), 2003-2008

Financial Year	Overall EU M&A		Europe PE M&A		
	Value (\$mil)	Deals	Value (\$mil)	Deals	% of Total
2003	504,009.1	10,076	83,707.9	757	16.61
2004	839,838.2	12,675	149,640.9	1132	17.82
2005	992,496.7	10,715	171,949.5	1206	17.32
2006	1,320,256.7	12,603	280,361.4	1725	21.24
2007	1,592,773.9	14,647	247,004.1	2081	15.51
2008	1,140,204.6	13,541	96,774.9	1551	8.49

Source: Thomson Reuters

According to the statistics of the European Private Equity and Venture Capital Association (EVCA), investments by European PE and venture capital firms amounted to € 73.8 billion in 2007, and approximately 5,200 European companies received private equity investments. European leveraged buy-outs in 2006 amounted to € 160 billion, an increase of 42% on 2005. With the usual leverage ratio of 1:3 or 4, this corresponds to a buy-out capacity of € 640 billion in 2006.⁷ Therefore we can assume that PE plays a significant role for industrial change in Europe, affecting a large number of mid-sized and large companies.

How Private Equity works



Source: Own – based on AT Kearney, 2006

⁶ World Economic Forum (2008): "Globalization of Alternative Investments. The Global Economic Impact of Private Equity Report 2008", Working Papers Volume 1, p. 16.

⁷ Van den Burg / Rasmusen (2007): p. 14.

PE actors as involved in the case studies

Fund	Headquarter	Foundation	Capital	Rank PEI 50
Permira (case studies Dinosol and Marazzi)	London	1985	\$ 25.43 billion	8
<i>Profile and investment characteristics</i>	Permira has a strong focus on the European market. According to the 2007 annual report Permira has investments in 23 companies with a total firm value of € 70 billion and approximately 220,000 employees. 20 of these companies are based in Europe, with a focus on Great Britain. Significant investments are: Dinosol, Cortefiel (both Spain), Saga/AA, Birds Eye Iglo, Gala Coral Group (all Great Britain), Debitel, Cognis, ProSiebenSat1 (all Germany), Valentino Hugo Boss, SEAT Pagina Gialle (both Italy), Maxeda (Netherlands) and TDC (Denmark).			
Enterprise Investors (case study Zelmer)	Warsaw	1990	\$ 1.1 billion	Not ranked
<i>Profile and investment characteristics</i>	Enterprise Investors investment activities began with the establishment of the \$ 240 million Polish-American Enterprise Fund in 1990. PAEF was funded by the US government to support the Polish private sector through direct equity investments and loans, primarily to small and medium-sized Polish businesses. Since 1990 Enterprise Investors has been managing one of the largest groups of private equity and venture capital funds in Poland and the Central and Eastern European region, with capital provided by major European and US financial institutions.			
Private Partners Equity (Case study Marazzi)	Milan	1994	n/a	Not ranked
<i>Profile and investment characteristics</i>	Private Equity Partners S.p.A is an independent Italian financial company, registered under Italian banking law, that provides investments in equity capital in unlisted companies, both directly using its own capital and through funds managed by its SGR.			

Source: Wilke, Maack and Partner

2.2 Hedge Funds

A hedge fund is an investment fund that is permitted by regulators to undertake a wider range of investment and trading activities than other investment funds. There exist a lot of different hedge funds strategies which determines the type and the methods of investment. As an asset class Hedge funds invest in a broad range of investments including shares, debt and commodities. Often hedge funds try to hedge their risks by using a variety of methods, for example short selling. Today the term "hedge fund" is applied also to funds that do not hedge their investments.

There is no definitive estimate of the assets under management by hedge funds. The major commercial data bases track between about 5,600 and 8,300 hedge funds. One estimate was that hedge funds in 2006 managed some \$ 1.3 trillion based on figures from around 6,000 single hedge funds worldwide.⁸ According to estimates in 2007 hedge funds managed some \$ 1.7 trillion with around 6,900 single funds worldwide.⁹ Similar to PE the US is still the dominant region for HF activities. HF based in the US accounts for more than 68% of the total capital under management. Nevertheless HF activities in Europe are becoming more important and accounted for 25% of the global HF industry in 2007.¹⁰

Following the "Hedge Fund Asset Flow & Trends Report 2006 – 2007", "Europe continued to be the fastest growing major investment region for most hedge funds. Total assets in funds which invest primarily in European markets increased at a rate of 46% in 2006 to \$ 276.5 billion - 64% of the \$87 billion increase was from new allocations".

⁸ Figures are based on the HF database, managed by HF Research INC.

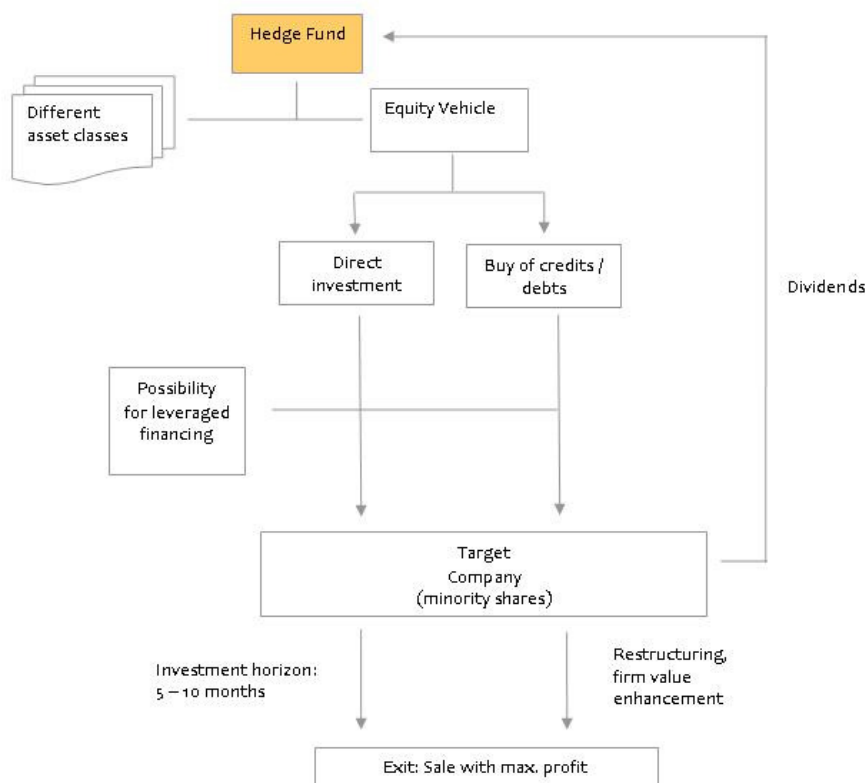
⁹ Van den Burg / Rasmussen (2007): p. 14.

¹⁰ Ibid.

However, HF equity holdings are only a small fraction of the total assets under management. They are by definition open for all kind of investments, in markets like bonds, derivatives and others using short-term strategies including day trading and the exploitation of very short term pricing anomalies (arbitrage).

Due to the frequent short term investments of hedge funds it is almost impossible to make any estimate in how many European companies they are invested in. Most of the activities and investments by hedge funds will be only relevant for those companies listed at the stock markets in Europe. However, hedge funds also act as buyers of company loans and can invest directly in companies. They can use very diverse investment strategies reaching from behaviour as active investors to completely opportunistic investment strategies.¹¹

How Hedge Funds work



Source: Own

The examples for HF activities we present in our case studies are active investments in a listed company and a case of buying a large company loan by HF investors.

¹¹ An opportunistic investment strategy is an approach that seeks to produce the greatest possible returns by making aggressive investments in the most-efficient products at a given time. Such funds typically hold their investments for five to 30 days, based on the momentum of the investments' values. Definition by HedgeCo.Net

HF and active investors as involved in the case studies

Fund	Headquarters	Founding Year	Capital
Wyser-Pratte Investment Management (Case study KUKA)	New York	1991	\$ 150 million
<i>Profile and investment characteristics</i>	The firm concentrates on investing in undervalued companies and follows an active investor strategy, thus Wyser-Pratte cannot be characterized as a classic hedge fund. Over several years Wyser-Pratte has focused on investing in several European companies. In Germany Wyser-Pratte became known through investments in Rheinmetall, Mobilcom and TUI.		
BlueBay (Case study Scheffenacker)	London	2001	\$ 21 billion
<i>Profile and investment characteristics</i>	BlueBay is one of the largest independent managers of fixed income debt funds in Europe. The company is listed at the London Stock Exchange. According to company information the focus of BlueBay is on European financial markets. In 2008 BlueBay had US \$16 billion under management in Europe, the only region where BlueBay makes direct investments.		
Davidson Kempner (Case study Scheffenacker)	New York	1990	n/a
<i>Profile and investment characteristics</i>	Davidson Kempner Capital Management LLC is a hedge fund management company which invests in public equity and fixed income markets across the globe. The firm makes its investments in distressed debt and stocks of companies that are undergoing corporate restructuring, including mergers, spin-offs, liquidations and recapitalizations. It also utilizes event-driven strategies including merger arbitrage, long/short, and convertible arbitrage strategy to select its investments.		

Source: Wilke, Maack and Partner

2.3 Sovereign Wealth Funds

A SWF is a state owned investment fund which can include all kind of financial assets such as stocks, bonds, property, precious metals or other financial instrument.. Over the past decade these kinds of funds have rapidly grown in importance and are now an important source of investment and market liquidity. Today, more than thirty countries have SWFs, with twenty new SWFs created since 2000. Typically, SWFs portfolios include a wide range of financial assets, including not only fixed-income securities but also equities, real estate and alternative investments. The assets managed by SWFs today are estimated at \$ 3 trillion.¹²

Most of these SWF investors were established in countries that are rich in natural resources like oil, for example countries from the Arab Gulf region, Ex-Soviet Union countries or Norway. SWFs are increasing much of their exposure to European equities indirectly, through investments in HF and PE. Ernst & Young estimate that SWFs account for 10% of all PE investment in recent years, and that this share is expected to grow.¹³ Prequin reports that the average current SWF allocation to HF is 7%, and that the average target allocation is 9%.¹⁴ SWF impact on industrial change in Europe is thus increasingly being indirectly channeled through these other paths.

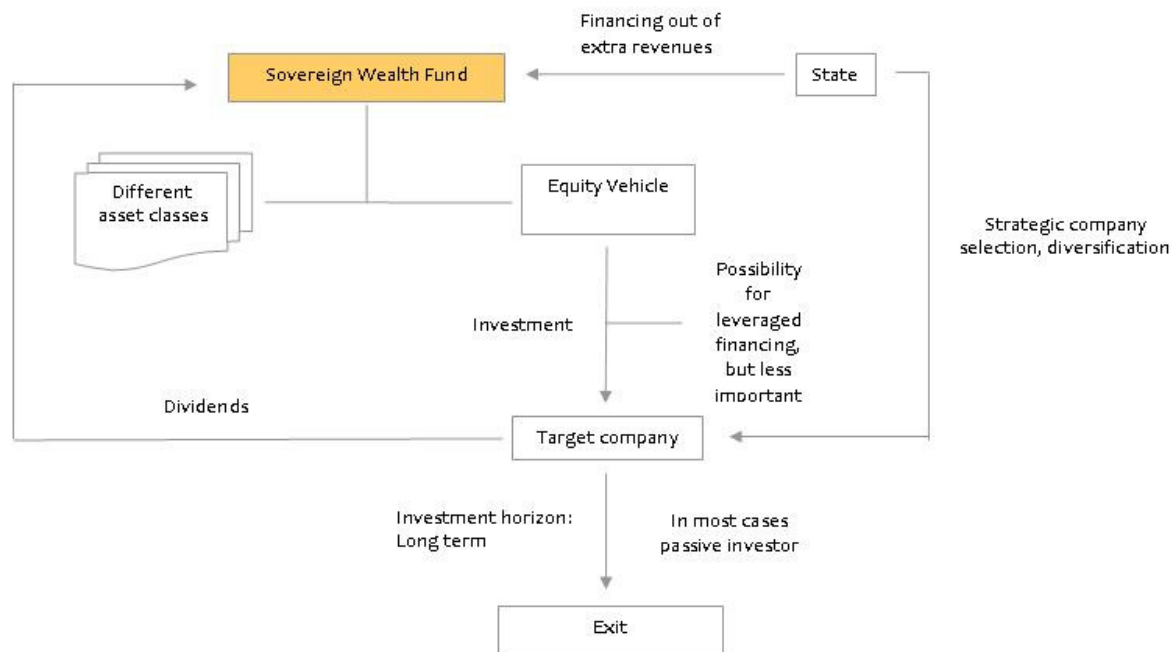
A list of the most relevant SWF actors and their investment activities in Europe is not available. However, one can observe that investments by SWF are mainly relevant for large companies. Most of the investments are concentrated in a small number of European countries (France, Germany, Great Britain, Italy etc.) and in a limited number of branches (banks, heavy industry, logistics, etc.)

¹² See: Morgan Stanley (2007): How Big Could Sovereign Wealth Funds be by 2015 and Gerard, Lyon (2007): State Capitalism: The Rise of Sovereign Wealth Funds, in: Journal of Management Research Vol. 7 (3).

¹³ Ernst & Young (2009): InterChange Vol. 23 (March), p. 11.

¹⁴ Prequin (2009): Hedge Fund Investor Spotlight. Sovereign Wealth Fund Issue, Vol. 1 (4), p.3.

How SWF work



Source: Own

SWF which can be found in the case studies

Fund	Origin	Founding Year	Capital
Qatar Investment Authority (Case study Cegelec)	Qatar	2003	\$ 62 billion
<i>Profile and investment characteristics</i>	To be less reliant from their oil and gas revenues in the future the QIA have several investment vehicles which are active globally. Beside equity investments QIA also invests in real estate through their investment company Qatari Dia. Significant European investments are the equity stakes in the London Stock Exchange, Barclays and the supermarket group Sainsburys (all in Great Britain).		
Dubai World/DP World (Case study P&O)	Dubai	2006	n/a
<i>Profile and investment characteristics</i>	Dubai World is a sovereign wealth fund launched by the government of Dubai. Dubai World plays a significant role in the creation of projects among the top companies in the Middle East. Their main focus will be on new areas of growth, such as media, healthcare, tourism, property, energy, industrial, research and humanitarian-related projects. Around 50% of their investments are in North America and the remaining in Asia. Dubai World functions as a holding with several investment companies under its umbrella, e.g. DP World. This company is one of the largest marine terminal operators in the world, with 49 terminals and 12 new developments across 31 countries. It was established through the merger of UAE-based Dubai Ports Authority (DPA) with DPI Terminals in September 2005.		

Source: Wilke, Maack and Partner

2.4 Conclusion

During the past decades a growing number of investments in European companies by private equity, hedge funds and sovereign wealth funds can be observed. However, it is not possible to give exact numbers in how many companies the different types of funds are invested. For PE we can assume that PE companies are invested in more than

10,000 companies of all size in Europe. For hedge funds no estimate can be made, but the typical hedge fund investment is in a listed company.

SWF are directly invested in a much smaller number of companies. The typical SWF investment is in larger companies, either as a majority investor or as an important minority stakeholder.

3 General remarks on the functioning and business models of Private Equity, Hedge Funds and Sovereign Wealth Funds

It is important to stress that private equity, hedge funds and sovereign wealth funds in general are following different business models which also influence their behavior and specific expectations as investors and/or owners. As already said, there are important differences with regard to aspects such as main investment focus and the investment horizon/duration. While for example hedge funds are similar to private equity funds in the way they obtain finance and use leverage, both types of funds differ significantly in the type of investment made and in the time horizon, which in the case of hedge funds tends to be much shorter-term and focuses more strongly on liquid financial assets. In contrast to both these types of funds, sovereign wealth funds generally follow a long-term agenda which has not only financial but also national economic policy goals.

It is important to differentiate between two different styles of investment behavior – *passive* and *activist* – which also is not necessarily determined by the fund type. Although most sovereign wealth funds are regarded as rather “passive” investors with little direct involvement in management decisions, and while private equity and hedge funds have much more activist investment styles, there are in fact different varieties within each type of fund in reality. The following table summarizes major basic aspects of the different business models of the three types of funds.

Basic characteristics of PE, HF and SWF business models

Aspect	Private Equity	Hedge Funds	Sovereign Wealth Funds
Investment focus	Primarily private and public equity	Broad variety of asset classes, like options, futures, commodities, currencies, and also investment in private equity	Broad variety of asset classes, amongst them investments in private and public companies
Ownership orientation	In most cases majority shareholder orientation	In most cases minority shareholder orientation	Both orientations
Investment horizon	Investment periods of 5 years and more	Average initial lock up period of 10 months or less	Long term investment
Selection strategies for investments	Undervalued companies with inefficient management; possibility to purchase stakes from large shareholders (families, state); free cash flow; breakup and sale potential	Undervalued companies with a story of take-over targets, breakup and sale potential; also buyer of distressed securities	Large variety – in contrast to PE and HF not only financial strategies but also national (economic) policy orientations are important in this context
Different stages of company development	Early, medium as well as late stage investments	Large variety – HF are largest buyers of distressed securities	Focus on medium stage investments

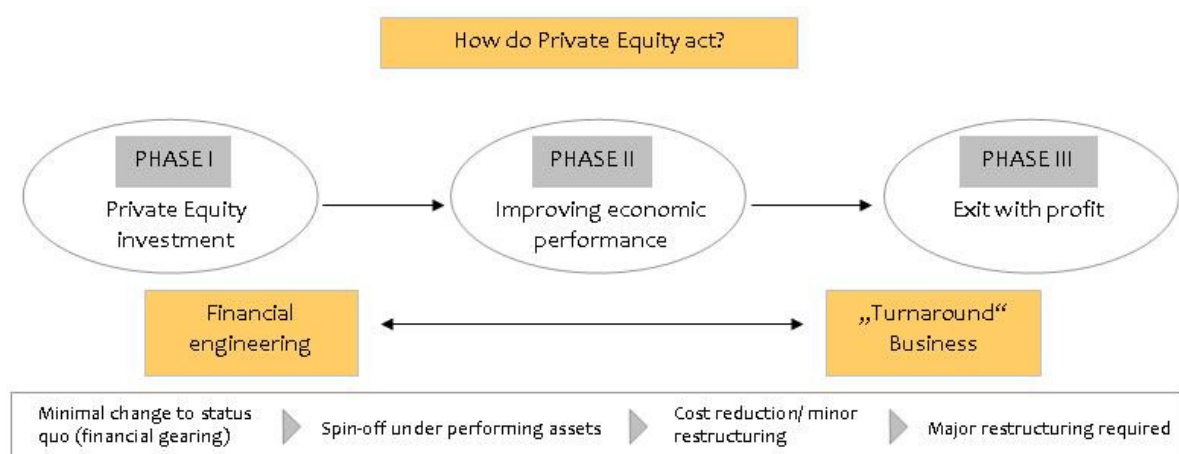
Exit strategies	Important and part of the investment strategy	Possibility of short term exit important/ dominant	Not defined
Reward system for fund manager	High performance based compensation	High performance based compensation	Not known
Determination of performance	Final valuation at exit, based on the final cash flow from the investment portfolio	Periodically, based on the net asset value of the investment via marking to market and on dividend paid	Periodically and long term, based on dividend payment and long term market value
Investment behaviour / influence on management decisions	Activist investor in most cases	Generally rather indirect influence but also cases of activist investors	"Patient" capital – in a generally passive type of investor
Strategies for the company invested	In most cases clear strategy, e.g. growth, turnaround, restructuring	Clear strategic orientation only in cases of activist investors	Strong interest in long term competitive and financial base of the company
Using of leverage instruments	Yes, often used	Yes, possible	Less important
Return objectives	Strong, short and medium term	Strong, short term	Weaker and long term

Source: Wilke, Maack and Partner, based on Achleitner, Betzer, Gider, Investment rationales of Hedge Funds and Private Equity Funds in the German Stock Market, December 2008, p.33.

Therefore we expect to find in the case studies that HF, PE and SWF follow different investment strategies even when investing in the same company.

HF are active from a position of a minority stakeholder who needs other investors to put pressure on the management for restructuring. Investment decisions by hedge funds typically take place in companies with a higher degree of ownership fragmentation. This is a result of liquidity considerations. Companies attractive for HF investments should have high dividend potential or an interesting short term M&A perspective which opens opportunities for a rise of stock prices. As a consequence of the predominant business model of HF it seems most likely that they force the management to implement measures which are oriented toward short term value creation.

PE mostly buys majority stakes in companies. They are often an exit opportunity for the former owners (families, state and even other PE firms). To buy a majority from a limited number of shareholders limits the acquisition risks. In the acquisition process PE on a regular basis use the possibilities of leveraged financing. PE funds select their target companies not only by price criteria but also by the criteria for leverage increases and stable cash flow capacities. PE investors use their majority control for three types of restructuring in the companies they have bought. First, immediate steps to improve the company's cash situation by selling operations and assets which are not directly linked to the core business. This free cash is used for a capital payback. Second, they do some financial reengineering to shift the purchase costs to the company. Third, they start business restructuring efforts to improve the long term potential of the company.



Source: Own based on ATKearney 2006

For SWF it does not seem possible to identify such a clear investment logic which leads to a distinct and unique business model for these funds. However, it is evident that they act in most cases as long term, patient investors who do not intervene actively to influence management decisions. Another distinguish feature (at least for the SWF from less developed countries) is the linkage between their goal as financial investors and national economic development policy.

Beside these general differences *between* the funds it is also important to stress differences *within* certain types of funds and differences with regard to the role of these funds in different stages and situations of business development, e.g. a start-up situation, growth phases, mergers and acquisitions, turnaround and crisis situations. Since these forms of business development all either will follow or result in industrial change at the enterprise level it is important to assess the role of the three types of funds, also taking into account the different stages/situations of company development.

Due to the fact that these different business models of the funds and different investment styles also will determine and influence the behaviour of the funds as investors and owners it is very difficult to draw simple general conclusions with regard to the impact of the three types of funds on industrial change and restructuring.

4 Dimensions of industrial change and the impact of PE, HF and SWF

4.1 Methodological remarks: How can we analyse impacts at the company level?

With regard to the impact of capital funds on industrial change and restructuring, in the context of this report the main focus is on the impact at the company level. Economists know that the impact of an investment on a company depends on many factors: the stage of development the company is in, the amount of money invested, the ownership structure and others.¹⁵ For example, the type of owner from which the portfolio company is acquired clearly makes a difference. Possible cases are:

- The family owned company (generally an SME), which is held by one or a small number of owners. One frequent motive for selling the firm to another owner in these cases can be a successor problem.

¹⁵ See for example the study by Kamp, Lothar / Krieger, Alexandra (2005): Die Aktivitäten von Finanzinvestoren in Deutschland. Hintergründe und Orientierungen.

- A subsidiary of a large diversified company, which may be exiting a specific country/region or product market. A frequently-stated motive for such divestment in the past decade has been pressure for more shareholder value through concentrating on core competencies and selling-off of non-core product lines.
- A government, which may be undertaking a program of privatization of public services or production.
- A stock-market listed company, which can be influenced in its strategy by acquiring a minimum proportion of shares in the company.
- A PE portfolio company (so-called "secondary buyout"). A PE firm may seek a buyer to exit its investment
- In all of these cases the specific conditions have a strong influence on the behaviour of the investing fund and also on the impact on the companies.

But these are not the only factors which determine which room for manoeuvre and effects an investment by a fund might have. As important as internal conditions in the company are the characteristic and strategies of the investing fund itself. As we have argued the investment strategies and the economic rationales of PE, HF and SWF are different and they have distinct investment motives. For example, HF, PE and SWF substantially differ with respect to investment horizon. Usually money in PE funds is locked up for an average period of 10 years, whereas money invested in HF can be withdrawn much more quickly. Investment horizons of SWF can be decades.

Additionally direct investments in companies play a different role for the three types of funds. PE is specialized in equity investments. However, equity investments only represent a small part of most HFs portfolios. And SWFs invest in PE funds and hedge funds in addition to direct investments in companies in their portfolio.

Even more important for the impact on the company is the question of how active the fund is as an investor. An activist investor approach is typical behaviour of PE investors. But we can also find this approach at some hedge funds and SWFs.

In the case studies we gather information on various dimensions to assess the impact. However, we are always confronted with methodological problem which can be described as the "*question of the counterfactual*":

"What would have happened to the company concerned, or the economy more generally, in the absence of PE involvement. Where we have data on company performance, against what benchmark should it be measured? How do we account for the fact that the companies taken over by PE are far from being a random sample?"¹⁶

Any study of the effects and impact of a specific phenomenon such as alternative investment funds would need to establish what difference that factor makes. Information and data on industrial change in companies with alternative investments therefore needs to be compared with data on other similar companies which have not changed ownership. Such comparisons are sometimes made with trends in the whole economy, but should be made between companies in the same sector – otherwise the comparison may simply reflect the fact that companies with private equity investors are for example in faster-growing sectors.

We have build three broad dimensions to measure impact: company performance, changes in employment and labour relations and other factors like effects of transmission to the whole branch and others.

The impact on business reorganization and employment should be valued both in quantitative (number of jobs) as well as qualitative terms (wages, working conditions, labour relations). This dimension includes "restructuring" and the permanent need of compa-

¹⁶ Watt, Andrew (2008): "The impact of private equity on European companies and workers: Key issues and a review of the evidence", *Industrial Relations Journal*, Vol. 39(6).

nies to adapt to changes in demand, the introduction of new practices or the arrival of new competitors which are necessary to remain competitive.

The following table summarises major topics and issues of concern reflected in the debate on enterprise level impacts of the three types of capital funds.

Impacts of capital funds on industrial change at company level

	Company performance	Employment and labour relations	Other impacts
Positive	<ul style="list-style-type: none"> - Efficiency and profitability - Value creation - Financing growth strategies - Availability of financial resources - Adaptability and innovation capacity - Management capacities and corporate governance 	<ul style="list-style-type: none"> - Employment growth - New opportunities for employees in terms of career development, training and competence - New forms of employee participation (including financial participation) 	<ul style="list-style-type: none"> - Acceleration of necessary industrial change - Increasing economic efficiency and competitiveness of companies as well as industry sectors - More efficient models of corporate governance and management
Negative	<ul style="list-style-type: none"> - No "real" value creation - Lack of long-term objectives - Wrong decisions due to single minded profit orientation - High financial burden / externalities - High risk strategy and danger of insolvency due to the use of leverage 	<ul style="list-style-type: none"> - Job losses due to accelerated restructuring also in profitable firms - Wage cuts and extending working time resulting from the need of higher profit goals and transfer payments - Lack of longer-term investment in human resources - Weakening of employee information and consultation - Lack of information and transparency - Weakening of national models and traditions of labour relations 	<ul style="list-style-type: none"> - High social burden due to accelerated restructuring - Decrease in national autonomy and weakening of national patterns of value creation and economic development - Increased instability of the financial market due to the use of leverage - Shareholder value orientation instead of taking into account stakeholder and further interests

Source: Own

To analyse for our case studies these three dimensions of impact we have filtered from the existing research and discussion the following hypothesis on the consequences of investment of PE, HF and SWF at the company level.

4.1.1 Restructuring, firm performance, profits and value creation

As rational investors PE, HF and SWF must be interested in improving company performance, resulting in rising profits and a visible value creation. To achieve these goals normally a process of change, investments and restructuring is necessary. Depending on the actual situation of the company this process can include a broad range of measures: separation and sale of less profitable branches of a company, investment in new products, growth of research expenditure, changes in management, cost saving programs etc.

After a period of restructuring performance, profits and value of the company visibly should improve. For HF this period should be rather short term (5-10 month) and value orientated. For PE the period of value creation will be longer (5 years and more) with the attempt to refinance the purchase price by using free cash flow of the company and realising a profit through a much higher sales price when exiting the investment.

However, the usage of free cash flow and debt leverage will burden the company and will create strong economic pressure to meet profit expectations. This might increase the need for further restructuring.

4.1.2 Impact on employment and labour relations

The effects of private equity and other funds on the employment development in target firms is probably the most controversial issue. From an economic point of view it is necessary to distinguish between the short term and the long term effects as well as between the direct and the indirect effects. Private equity associations and other groups accentuate the long term positive effects of private equity on employment which are linked to the expectation of improved growth and profitability of the companies. Other researcher and critics of PE stress the short term effects of restructuring which often can lead to redundancies and unemployment. In general its is very complicated to make for PE investments a numerical assessment of jobs created through growth, jobs transferred to other companies by splitting companies and selling part of the holdings and jobs lost by restructuring processes. Therefore it is no surprise that empirical studies came to very different results and conclusions.

Both with regard to hedge funds as well as sovereign wealth funds there are no studies known so far analysing the employment effects of these funds at the firm level.

If restructuring at the company level in many cases accompanies an investment by PE, HF and SWF the question is how this affects wages and working conditions. Similar to the issue of job creation, the impact of alternative investment strategies on wages and other aspects of work are highly controversial and there is great variation between the messages of business orientated surveys and studies on the one hand and more critical studies on the issue, which often are based on case study evidence.

A recent survey amongst 190 private equity-owned companies that were subject to a buyout between 2002 and 2006 conducted by the Centre for Management Buyout Research (CMBOR) on behalf of the European Private Equity & Venture Capital Association (EVCA) has drawn an overall positive conclusion with regard to the impact of private equity on working conditions and labour relations.¹⁷

Most findings rely on case study evidence mainly which have been carried out during this decade in particular by trade unions and other "critical" institutions, e.g. the Hans Boeckler Foundation in Germany.¹⁸ In these case studies it is reported that workers often have been forced to accept pay cuts and other reductions in working conditions.

One would also expect growing tensions and disputes between trade unions, management and interest representatives of the employees on the course of restructuring and the possible burden for the different stakeholders.

Similar to the issue of wages and working conditions there has been hardly any significant research on the impact of PE, HF and/or SWF investments on social dialogue and information and consultation practice at the company level. Since also the capital fund industry itself has shown no real interest in this issue, our knowledge on this topic mostly relies on reports by trade unions, works councils and in the context of – trade union orientated – case study work.

There is evidence that the concrete economic situation and the position and role of the works council and trade union structures at the company level to a large degree determines the development of social dialogue and management-employee relations. This is

¹⁷ EVCA/CMBR (2008): "The Impact of Private Equity-backed Buyouts on Employee Relations", Research Paper.

¹⁸ Faber, Oliver (2006): Finanzinvestoren in Deutschland. Portraits und Investitionsbeispiele, Düsseldorf, Hans-Böckler-Stiftung, Arbeitspapier 123. Further case study reports and company statements are available on the homepage of the Foundation. www.boeckler.de.

also the case after a capital fund takeover or majority investment. Where trade unions and/or works councils have a strong organisational position they often can bargain effectively with new investors. Also national traditions are likely to be relevant, as case study examples in Germany illustrate: Even in the case of corporate turnarounds there are cases where private equity funds have regarded works councils as a positive resource and actor.¹⁹

4.1.3 Other impacts: Management practice, corporate cultures and governance

A review of management practice in private equity backed companies gives some evidence that there are changes in management practice and governance rules:²⁰

- There is a growing influence of performance-based reward systems and regular performance appraisal.
- A faster introduction of lean management and production concepts like self managed teams, individual communication, training, and making workers responsible for their own jobs and advancement.

4.2 General remarks on existing research and analyses

Estimates of the “real” impact of funds investment on companies (employment and other impacts such as wages, profits) vary quite widely from quite positive to negative.²¹ In particular the literature on *private equity* is most extensive. These studies have focused on a variety of outcomes, including returns for investors in private equity, and the employment, sales and profitability outcomes of private equity investments in portfolio companies. Beside literature with a broader scope there are also studies which focus on concrete case studies.

Relevant literature on *hedge funds* is less extensive, and due to the lack of transparency regarding most hedge funds investments, focuses mainly on returns to investors. Some recent econometric work, however, has looked at significant shareholdings by hedge funds in listed companies. There is only very limited literature regarding the influence of hedge funds on employment issues. Research about hedge funds activism and effects on industrial change, i.e. restructuring and employment is still not very broad. One study is known which focuses on the U.S. as well as Europe.²² For Germany also only one general study is known.²³ Admittedly these studies focus mainly on the companies’ value and their development on the stock markets after the hedge funds acquisition.

Finally, scientific interest in *sovereign wealth funds* has been quite recent. The literature here is quite thin, particularly on econometric studies on the impact of sovereign wealth funds investments. At this time no studies are known dealing with effects of Sovereign Wealth Funds on employment topics or industrial change in general.

Most existing studies are focussing on the issue of financial outcome and only very few research have been done on the impacts of funds on wages and working conditions, or on the influence of such investments on the coordination with worker representation. Concerning such issues case most results can be drawn from case studies because overall empirical studies are missing.

¹⁹ See Scheytt, Stefan (2006): Glück im Unglück, Die Mitbestimmung, No. 6, 2006, p. 10-15. The article describes the experience of the employees at MTU Aero Engines in Bavaria with the Private Equity Fund KKR.

²⁰ Thornton, Phil (2007): Inside the Dark Box – Shedding a Light on Private Equity. London, Work Foundation.

²¹ For a more detailed review of literature and research on the impacts of the three types of funds see the parallel study for the EESC: Voss (2009).

²² Stockman, Nick (2007): “Influence of hedge funds activism on the medium term target firm value”, Working Paper University of Rotterdam.

²³ Holler, Julian and Bessler, Wolfgang (2008): “Capital markets and corporate control: Empirical evidence from hedge fund activism in Germany”, Discussion Paper University of Giessen.

PART II:

CASE STUDIES

5 Overview and methodological approach

In the following we briefly analyse first for each country the existing statistical information on PE, HF and SWF investments. For PE the statistics are quite good and allow a comparative analysis. For HF we can only report larger investments in listed companies. Also for SWF only investments in listed companies are available.

Confronted with the large number of companies from which our case studies could be drawn, in combination with the difficulties of comparing companies and investment behaviour of funds, we set up the following design for selecting our case studies.

- ☐ First we tried to analyse the relevance of PE, HF and SWF in the six countries specified (based on a brief literature study for each country and existing overviews – see also the country based figures for PE, HF and SWF presented in the annex).²⁴
- ☐ Secondly, we identified and pre-selected 10 possible relevant cases in each country (including information on the branch the company comes from and the type or fund).
- ☐ From this list we chose one case per country (in the case of Germany two companies for case studies).

The final selection of a case also reflected criteria such as:

- ☐ Selecting companies with a certain size (national) public prominence;
- ☐ cases from different sectors like manufacturing, retail, services, construction etc.;
- ☐ companies which have been acquired at a sufficient time in the past, e.g. two to four years ago, so as to give sufficient time for examination of consequences;
- ☐ cases with involvement of either PEF or HF or SWF;
- ☐ both listed and non listed companies.

The final selection of case studies includes two investments of SWF, two of hedge funds and three of private equity funds in the six countries. In this sample we also cover very different strategies followed by the investing funds (activist investor approach with clear restructuring goals, typical PE investments with financial engineering, long term investment linked to national development strategies, etc.). We also cover complete take-overs as well as minority investments. And we see investments in very different stages of company development.

In most cases the investments have not yet been exited. The following table give a first overview on the cases.

²⁴ See for example the list of cases in Germany named in the study by Krieger / Kamp (2005).

Chart on case studies

Name	Country	Branch	Investor type	Name	Shares	Volume of transaction	Sold by
Cegelec	France	Construction and service	SWF	Qatar	100%	€ 1.6 billion	PE
P&O	United Kingdom	Logistics	SWF	Dubai	100%	\$ 6.8 billion	P&O
Marazzi	Italy	Pottery	PE	Permira and others	33%	€ 250 million	Marazzi
Zelmer	Poland	Household appliances	PE	Enterprise Investors	100%	N/a	State
Dinosol	Spain	Distribution	PE	Permira	100%	€ 800 million	Ahold Group
KUKA AG	Germany	Automation/robotics	HF/ Raider	Wyser-Pratte and others	9%	€ 11 million	Shares traded at stock market
Scheffacker AG	Germany	Automotive supplier	HF	Blue Bay and others	70%	€ 300 million	Debt to equity deal

After these first indications on the relative national importance of these investments we describe and analyse in detail the investment and the consequence in the different case studies. We have tried to organize all case studies in a comparable way based on a standardised data/information set up including pre-designed questionnaires for interviews with various stakeholders. If possible we had interviews with company representatives, fund manager and employee representatives/ trade unions.

However, as always with case study work it includes a good deal of story telling which makes it difficult to compare the cases one by one.

6 Marazzi/Italy: A case of PE investment

6.1 Overview of PE, HF and SWF investments in Italy

PE activity in Italy has been less significant than in other major European economies, peaking in 2006 at 0.33% of GDP (in terms of PE investment in Italian companies) and 0.23% (in terms of Italian-based PE investment activity). Investment in the seed and startup stages has been weak throughout the period, and buyout has been very dominant throughout the period (peaking at 88% of activity in 2007).²⁵

The most significant HF activity has been concentrated amongst the largest listed Italian companies, in only two of the top 20 investments accounting for more than one percent of shares outstanding.

With the exception of Abu Dhabi's investment in Mediaset (2% of shares outstanding) the top 20 SWF equity positions in listed Italian companies are accounted for by Norges Bank.

6.2 Marazzi – Private Equity allows growth strategy for international expansion

Introduction: why the case was selected

To select the case of Marazzi we screened a large number cases of PE investments in Italy. The final decision to analyse the PE investment at Marazzi was based on the im-

²⁵ See the figures for PE, HF and SWF investment in the back-up of the study

pression that this case is an example for a former family owned company which was looking for new models of partnership and financing structures to grow from a leading European company to a world leader in its markets. In the case of Marazzi the first transaction with the involvement of PE was in 2004.

The investment by Permira and Private Equity Partners had the clear intention to bring the company to the stock market and to invest into new markets. At this time Marazzi had about 4000 employees in 18 production sites in Italy, Spain, France and the US.

After taking PE on board Marazzi grew fast by acquisition but also was confronted with new economic problems out of this process.

Because Marazzi originally is coming from a business district in Italy with a strong trade union tradition the case study can give additionally some insights in the position of Italian trade unions towards PE investments.

6.3 Profile of the company and the financial investors²⁶

The company Marazzi Group

Founded in the 1930s, Marazzi's international activities have constantly expanded since the 1980s. Marazzi is currently one of Italy's major multinational companies, the world leader in its sector – design, manufacture and sales of ceramic tiles, with a growing presence in sanitary fixtures. These global markets are dominated mainly by domestic competitors. The business model is vertical integration along the value chain, with direct control of the entire process (with some of the steps outsourced), systematic innovation in both design and technology, and control – or sometimes direct management – of distribution.

The Group, based in Sassuolo (Modena) in the region Emilia Romagna, has manufacturing plants in Italy, Spain, France, Russia and the United States. It employs 6.000 staff in its plants, commercial branches and showrooms.

The activities in Italy take place mainly under the brands Marazzi, Marazzi Tecnica and Ragno, as well as Hatria (with a factory in Teramo) which is dedicated to the production of sanitary products and bathroom furnishings.

The main foreign companies in the Marazzi group are:

- in the United States American Marazzi Tile of Dallas (Texas) and Monarch Tile of Florence (Alabama);
- in Russia Kerama Marazzi;
- in Spain Marazzi Iberia, based in the ceramic district of Castellón de la Plana;
- in France the Groupe Marazzi France.

The Group is also present in China with a local organization dedicated to the distribution of products in the Chinese market and in the Far East. Global tile consumption, which is predicted to reach approximately 9 billion square metres in 2011,²⁷ has seen constant growth in recent years (3.8%) thanks to increasing demand in Eastern Europe, Asia and the Middle East. Consumption estimates predict a global market distinguished by different levels of performance depending on the country: Russia and China are the countries where the fastest growth is expected.

The global tile market is not homogenous but rather a group of regional markets, with specific tendencies and dynamics, segmented into three levels: commodity, mid range and top level (where top level technology meets with highest design expectations).

²⁶ Case study is based on information provided by the management of Marazzi and Permira as well as by trade unions interview partners from CISL, CGIL and the Marazzi EWC.

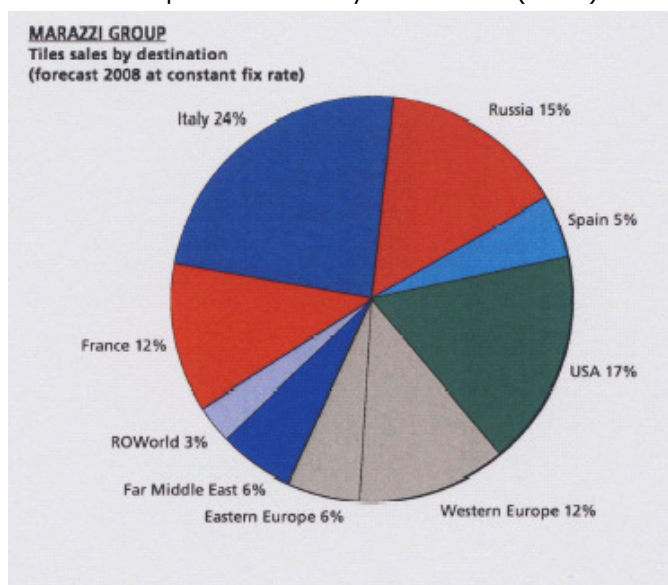
²⁷ Osservatorio Previsionale Confindustria Ceramica – Prometeia, May 2009.

While the mid range level has by now been displaced in the regional market, the top level remains dominated by Italian products and is still covered to a great extent by the combination of Italian production and export.

The group's global approach combined with its focus on local markets' needs form the basis of its global leadership in the tile sector. Marazzi has thus become the leading player in many of the most important international markets:

- ☐ leader in Italy, with a 12% market share;
- ☐ leader in France, with a 10% market share;
- ☐ leader in Russia, with a 8% market share;
- ☐ the second player on the US market with a 10% share;
- ☐ one of the main players in the Spanish, German, Scandinavian and Greek markets.

Marazzi Group: Tiles Sales by destination (2008)



Source: Marazzi Group

The financial investors: Permira and Private Equity Partners

Permira is one of the principal private equity investors on the international level, with offices in New York, Tokyo, London, Frankfurt, Milan, Paris, Madrid and in other European capitals. In 2007 Permira Funds had assets under management of € 21 billion. The last fund, raised in 2006, is Permira IV with € 11 billion, the largest in Europe at that time.

From 1985 to 2007 more than 280 investments were made by Permira funds. Permira Italia has participated in noteworthy operations, some a success (Valentino, Tecnolitica, Grandi Navi Veloci), others characterized by a strong speculative element and repeated secondary sale operations between investments funds (SEAT). In some cases the target company's large debt almost led to bankruptcy in the context of the recent financial crisis and the subsequent credit crunch, e.g. Ferretti (motor yachts), which Permira Italia exited from in 2006, selling it via a secondary sale to Candovar.

The second investor, Private Equity Partners S.p.A is a major independent merchant bank registered under Italian banking law. It was founded and is fully controlled by Fabio L. Sattin and Giovanni Campolo. It makes equity investments in unlisted companies, both directly using its own capital and by means of the funds managed by a sec-

ond company. Through this, Private Equity Partners also acts as a management company under Italian law of JP Morgan Fund III, which was underwritten entirely by international institutional investors and specializes in equity and buy-out investments.

With 20 years' experience, and more than 50 investments completed in Italy, Private Equity Partners, which currently manages its 4th Fund (Private Equity Partners Fund IV), is indisputably one of the leaders in the Private Equity sector in Italy.

6.4 The transaction

At the beginning of the transaction, Marazzi (since 2005: Marazzi Group) was controlled by the third generation of the original founding Marazzi family, which held the majority of the share capital. The acceptance of private equity fund investment in the company originates from mutual interest. In the first half of the decade the company found itself at a turning point in its history. It was already a world market leader, but it still would have to take a qualitative step forward to develop from a multinational corporation to a full-blown global player active in emerging markets as well. To this end, it needed not only more finance for expansion strategies, but also a "managerialization" of the company. On this basis the cooperation with private equity funds began: Permira has contacts in China and the United States, and Private Equity Partners is active in Russia and specializes in IPOs. In turn, the funds became interested in Marazzi not only because it was an already noteworthy brand within the sector and present it all segments, but also because it was a healthy company with significant growth prospects.

"When we analyzed Marazzi, which is a world leader in their sector and is already implementing the industrial polo strategy alone, we recognized them immediately as a company not to let escape, which we should enter into and discuss with its leader where it wanted to go".²⁸

The representative of the Marazzi family Filippo Marazzi sees the entry by the private equity funds as the leverage that, in addition to securing the finance necessary for the expansion strategies, will allow for the modernization of the management of the company and consolidation of leadership in the sector.

Last but not least, a common objective of the Marazzi family and the PE funds was to list the company on the stock market (IPO), which was seen as a fundamental strategic move to support the international development strategy of the company.

The investment of the two private equity funds in Marazzi is tightly connected to the strategic acquisition of Welor Kerama, the leading company in Russia. This company offered a rich network of stores throughout the entire country in addition to production facilities. In 2004 Welor Kerama had sales of about € 61 million with EDITDA of € 25 million (Marazzi Group, s.d.). Private equity played a key role in initiating and carrying through the transaction, since Private Equity Partners fund was involved in the Welor Kerama operation.

"We were working on the Welor operation independently of Marazzi (...). We were in contact with both the Russian entrepreneur and the management and we understood that those who actually had the power to decide were the managers. At the same time we knew that Marazzi had the intention of entering the stock exchange and bringing companies into the stock exchange after helping them grow is our specialty. Therefore we put two and two together and along with Permira we contacted Marazzi, proposing the Russian deal to them well, which in the meanwhile we studied in order to not displease the management. All in all we did what private equity should do and that is to bring tangible, concrete opportunities to the entrepreneur. I don't understand how you can think of getting 30-50 percent returns without a creative approach".²⁹

In turn, Filippo Marazzi explained it this way regarding the meeting with the private equity funds:

²⁸ Paolo Colonna (Per mira), quoted in: Peveraro, S. (2008): "Private equity e aziende familiari. Dieci storie raccontate dai protagonisti", Milano: Egea, p. 73.

²⁹ Fabio Satin (Private Equity Partners), cited in: Peveraro (2008), p. 73-74.

"I decided make an IPO with the company, but I understood that it still wasn't the right time. I wanted to get there quickly and my delegated administrator at the time, Emilio Scheenberg suggested that we aim for private equity because a fund, taking an important minority stake of our capital, would accompany us in the initial IPO phase. For this he announced a beauty contest between funds, but I would tell them that after a short while I had lost hope in finding the right partners. Everyone that I met had only a financial approach and wasn't interested in understanding either the company or their objectives. Then it came time for Permira and Private Equity Partners and luckily their approach was totally different" remembers Marazzi, who said: "They talked about production, development prospects, and of course the stock market and how they could get there".³⁰

In December 2004 the private equity investor Permira and Private Equity Partners built a new company (Riaz) and bought from the Marazzi family (Filippo Marazzi und Rosaria Marazzi) 33% of the capital of the company (Permira 28% and Private Equity Partners 5%) with the aim of going public within the next three to five years. The volume of this sale was € 132 million (€ 3.89 per share), whereas the total value of the company was estimated at €750 million (annual turnover in 2003). Marazzi and the funds also agreed that, "in the case of the company's quotation and if the annual yield compounded yearly on the investment of Riaz in the company was higher than an agreed upon level, Riaz would have returned an additional premium to Filippo and Rosaria Marazzi, up to a maximum of € 40 million (equal, considering the number of shares originally acquired, to the maximum of € 1.18 per share)" payable with the net proceeds deriving from the sale of their own shares in the global offer.³¹

At that moment (December 2004) Marazzi had 18 plants in Italy, Spain, France and the US with a total amount of 4000 employees. As mentioned before, due to the private equity investment Marazzi was able to buy the Russian company Welor Kerama at the beginning of 2005. At the end of 2005 Marazzi had 20 plants and roughly 5,800 employees.

In February 2006 Marazzi went public (on the Blue Chip segment of the stock exchange). Permira and Private Equity Partners carried out the preparations, documentation and writing of the necessary documents for the quotation and the business plan. They also organized and managed the section of Sponsors and Global Coordinators (Morgan Stanley and Mediobanca). The company was quoted at € 10.20 per share on the basis of a valuation of € 974 million. In agreement with the company, at the time of quotation, the funds sold two thirds of their remaining post-quotation shareholdings, reducing their stake to 10% compared with the original 33%. These funds earned substantial profits on this sale, since Permira and Private Equity Partner bought the shares for € 3.9 each and sold them for € 10.25. Both investors withdrew from Marazzi in February 2007 with total profit € 134 million in two years. After the investors left the company the stock price rose to € 12 per share but then decreased to € 6 in 2008.

In May 2008 Marazzi was delisted in order to consolidate and expand the company. From the interviews given by Marazzi a certain delusion with regards to financial markets is apparent, which for long periods do not reflect the real value of his company. Company management emphasized how the stock market during the period Marazzi was listed was "schizophrenic", dominated by short-termism and by the consequent focus on quarterly results. The result was an undervaluing of Marazzi shares. On the other hand, company shares were repurchased from the market at a lower price than the initial quotation (€ 7.15 compared to € 10.25). Officially, the exit from the market was motivated by the necessity to return to concentrated ownership which was needed at the time to guarantee the necessary operational flexibility to carry out medium-long term investment programs.

³⁰ Filippo Marazzi, quoted in: Peveraro (2008), p. 71-72.

³¹ Peveraro (2008), p. 75.

Once again Permira and Private Equity Partner invested in the company (€ 250 million) and created jointly with Marazzi the new enterprise Fintiles.

In July 2008 a voluntary public tender offer launched by Fintiles S.r.l. for Marazzi ended successfully. Fintiles is a company indirectly controlled by Filippo Marazzi with 49% participation of Permira and Private Equity Partners (PEP) through LuxELIT. The offer was launched for 49,928,242 Marazzi shares listed on the Italian Stock Market, which represented 48.8% of company's share capital.

As of July 18, 2008, the last day of the offer acceptance period, 47,590,145 Marazzi shares were tendered, corresponding to 95.3% of the shares subject to the offer and 46.6% of the capital of Marazzi (represented by 102,232,000 ordinary shares) and an amount equal to € 340.3 million.

Taking into account the shares owned by Finceramica before the beginning of the offer, the offeror owns a total stake in the Company equal to approximately 97.7% as of the 25th of July. The table below summarizes the ownership structure of Marazzi and its changes between 2004 and 2009.

Marazzi Group: ownership structure 2004/2006/2008 (as of 31. December)

	2004	2006	2008
Finceramica SpA (100% Marazzi Family)	67%	50.92%	51%
Filippo Marazzi		5.87%	
Rosaria Marazzi		5.60%	
Riez: Permira	28%		
Private Equity Partners	5%		
Blue Ridge Capital*		2.58%	
Free Float		35.04%	
LuxELIT (84% Permira, 16% Private Equity Partners)			49%

* Relates to a financial investor considered as part of the free float

Source: Marazzi Group (2006, 2007, 2008a, 2009)

6.5 Strategy of the financial investors

Marazzi represents the (atypical) case of a private equity investment without debt leverage and a minority partnership (33% of shares) by private equity:

*"Although our investment logic is often in terms of majority ownership, in the case of Marazzi we made an exception, for the clarity of the project and the timetable of the operation"*³²

Emerging from the interviews is the fact that the decision not to use debt leverage was made together by Marazzi and the PE funds. Using debt leverage means that much of the cash flow of the acquired company has to be used for interest and amortization payments and therefore is not available for other uses. The case with Marazzi was different; the cash flow was good, but so were the prospects for growth, which still required enormous financial resources. On the part of the PE funds, the investment therefore was in the growth and the "globalization" of Marazzi. A growing company absorbs cash flows; in addition to the operation in Russia already mentioned other investments were scheduled in factories and or minority acquisitions. "What remained free would have been insufficient for an operation based on debt leverage".³³

Both the Marazzi management and the Permira representative interviews note the "Italian spirit" of the two funds that participated in the Marazzi operation. Permira Italia,

³² Paolo Colonna (Permira) cited in Pecoraro (2008), p. 73.

³³ Interview with company management.

even though a part of a global private equity fund, differentiates itself from other PE funds, even to some extent within the Permira group. This is connected to the origins of Permira and in particular of Permira Italia with respect to competitors. These are usually Anglo-Saxon funds which opened a branch in Italy entrusting it to two or three managers taken from investment banks or similar organizations (as in the case, for example, of Candovar). The founder of Permira Italia (Paolo Colonna) has been involved in the sector since the mid-1980s and in this time has acquired a lot of experience and become established in the area, forming a network with the main banks and Italian entrepreneurs. On this basis relationships with entrepreneurs were not purely financial, i.e. the links between Permira and the companies were not purely instrumental. In other words, the companies are not considered purely as "commodities". Rather, the relationship takes on more and more the characteristics of what can be defined as a "partnership for growth", which promises high earnings for all participants.

6.6 Consequences for the core business

As mentioned above, the use of private equity funds allowed Marazzi at the beginning of 2005 to buy Welor Kerama in Russia, a leading producer with 15% of the internal market and a wide sales network. This operation was part of a strategy of internationalisation, which Marazzi had always followed, namely entering new markets through the acquisition of important indigenous producers in order to produce locally for the respective market. This was already the strategy in the 1980s when Marazzi invested in the United States, and later continued its expansion through the construction of its own plants. The local production locations and sales networks in the principal outlet markets are among the principal factors in the success of the Marazzi group. In addition to proximity to the local markets, this strategy allows for the reduction of delivery times and transportation expenses, which are particularly high in this sector.³⁴ In this respect the entry of the private equity fund seems not to have had significant consequences for the core business in the sense of an abandonment or drastic change. As already highlighted, the entrance of private equity is intended instead to consolidate the development model followed until then by Marazzi, i.e. taking over leadership in new markets.

The investment of private equity without leverage has left the necessary flexibility to finance future acquisitions with debt, to bring already initiated strategic investments to completion (such as the doubling of factory capacity in Dallas, United States) and to gradually modernize systems in other factories. The latter confirms and reinforces the technological leadership of Marazzi in their own sector, which was achieved beginning with the use of tunnel kilns in the 1950s and above all with the revolutionary patenting of "monocottura" in the 1970s, which drastically reduced the production process from 24 hours to just one hour and subsequently became the most widespread production process in the world. This was followed the Firestream patenting (enameling on the incandescent support) in the 1980s. According to the company, Marazzi today depends on sophisticated systems, with high level automation and vertical integration, to guarantee productivity levels significantly higher than the sector average, as well as on new technologies (e.g. continuous production) tested by the Group since 2006, which allows for more productive flexibility and at the same time reduces the storage needs for the finished product.

6.7 Economic development of the company

These developments can be traced in the company's financial data, which is available up to the first quarter of 2008. With delisting in July 2008 the publication of data also ceased, and were also not made available. As a consequence only an evaluation of the

³⁴ In the words of the manager interviewed, "the tile business is 30% production, 30% design and 40% logistics".

four years from 2004-2007 is possible, i.e. prior to the early symptoms of the financial crisis in the United States which then expanded globally in October 2008.

With this limitation, there is no doubt that the period from 2004 to 2007 was a period of strong growth for the group (see table 2).

The results of the first year of the presence of private equity funds are extraordinary in many ways. The group ended the year 2005 with a net profit of € 52.8 million, compared to € 14.9 million in the previous year. Sales totalled € 903.2 million, up 19.8% compared to 2004 (+10.4% due to the Russian acquisition and +9.4% within existing operations). EBITDA increased by 50.5% in 2005 (+21.4% for the old consolidated operations), to € 159.7 million (17.7% of sales) versus € 106.1 million (14.1% of sales) in 2004. As of 31 December 2005 net financial debts were € 281.2 million (€ 263.0 million in 2004).

2006 had seen the best performance in the past decade. The key financial figures of the group achieved new records, with further growth over 2005, in spite of significant increases in energy costs and a slowdown in the US market. Revenues from sales in the year amounted to € 964.1 million, an increase of 6.7% on 2005. EBITDA, which amounted to € 179.6 million, increased by 12.4% compared to the previous year on the basis of a largely similar consolidation area. The margin percentage also improved significantly, to 18.6% compared to 17.7% in the previous year.

EBIT was also very positive and amounted to € 117.8 million (+14.5% compared to the previous year) and included restructuring charges in French operations of € 6.8 million. The net profit was also in strong growth (+10.6%), amounting to Euro 59.1 million for the year, compared to Euro 53.4 million in 2005.

As of December 31, 2006, net financial debt was € 203.2 million, a decrease of € 78 million compared to December 31, 2005 (€ 281.2 million) and € 8.9 million compared to September 30, 2006 (€ 212.1 million).³⁵ At year end, the net financial debt/net equity ratio decreased to 0.40 (compared to 0.68 at the end up of 2005) and the EBITDA ratio increased from 1.7 to 1.1 (Marazzi Group 2007, S. 10-11).

In 2007 the significant increase in the cost of energy resources and the strong contraction in the US market marginally impacted upon the operating result of the Group. Sales in the year were growing by 2.1% on 2006; EBITDA amounted to € 174.3 million, a decrease of 2.9% on 2006. The EBITDA margin was 17.7%. EBIT, which amounted to € 119.0 million, +1.1% on the previous year (+3.4% at constant exchange rates), maintaining a margin on revenues of over 12%. Net profit had significant growth (+4.5%), amounting to € 61.8 million for the year, compared to € 59.1 million in 2006.³⁶

As of December 31, 2007 net debt was Euro 230.4 million, an increase of Euro 27.2 million on December 31, 2006 (Euro 203.2 million) due to the acceleration of investments. At year end, the debt/equity ratio was 0.43 (0.40 at year-end 2006) and the EBITDA ratio increased from 1.1 to 1.3.

³⁵ “This reduction was mainly determined by the share capital increase which, with the Parent Company listing, contributed financial resources of €67.4 million, net of expenses and fees. The liquidity generated from the ordinary activities fully covered the investment requirements (€ 45.1 million), increased working capital (€ 24.6 million) and dividends (€ 20.6 million)” (Marazzi Group 2007, p. 10).

³⁶ “This positive result was achieved in spite of higher financial charges: in 2007 the strong appreciation of the Euro resulted in higher exchange rate losses of €2 million, while the interest rate movements, together with the high levels of investment in the year, resulted in higher financial charges of €6.2 million. The tax rate improved from 39.3% in 2006 to 31.4% in 2007 (despite 2006 had benefited from the positive effects resulting from the realignment between statutory and fiscal values of the fixed asset in the Italian BU for €4 million). The year 2007, in fact, benefited from the adjustment of the deferred tax liabilities to the new tax rates in force contained in the “2008 budget law” for Italy and from similar fiscal provisions in Spain; the total effect of the fiscal benefit was €8.4 million” (Marazzi Group 2008, p. 20).

Marazzi Group: key financial data in accordance with IAS/IFRS (€ millions)*

	2004	2005	2006	2007
Net Sales / Revenues	753.7	903.2	964.1	984.0
EBITDA	106.1	159.7	179.6	174.3
EBIT	50.0	102.8	117.7	118.9
Group Net Income / Net Profit	15.3	53.4	59.1	61.8
EBITDA / Sales	14.1%	17.7%	18.6%	17.7%
Net Working Capital	260.6	229.4	259.9	266.6
Fixed assets and other assets	542.1	611.9	585.3	614.3
Long-term liabilities	144.2	145.1	131.8	115.0
Net financial debt	263.0	281.2	203.2	230.4
Total shareholders' equity	392.7	410.9	504.5	529.3
Net equity per share (Euro)	3.82	4.3	4.9	5.1
Number of shares (in millions)	102.85	95.05	102.23	102.23
Net financial position/ Net equity	0.66	0.68	0.40	0.43
Operating cash flow	66.8	156.3	78.8	73.4
Amortisation & Depreciation	53.8	55.7	55.1	54.9
Cash flow for investments	(55.0)	(127.2)	(45.0)	(73.9)
Employees (average)	4,264	5,808	6,299	6,496

* Data are rounded to one decimal place

Source: Marazzi Group, as of 31 December

When considering certain data broken down by geographic area (see table 3) the key role of the acquisition in Russia becomes clear. The Russian business unit achieved stellar results year after year and contributed in a clear way to the overall positive performance of the Marazzi group: a 29.2% increase in proceeds in 2006 (against +6.7% overall) and 26.1% in 2007 (overall: +2.1%), with and EBITDA that in 2006 grew 30.7% (against an average of 12.4) and another 13.1% in 2007 (overall: -2.9%). This brought the profit margins of this business from 39.7% in 2005 to 40.1% in 2006 and then down to 36.0% in 2007.³⁷

"The high margins, compared to the other Business Units, benefit from the lower cost of a number of production factors and from the adoption of a different business model, based on a broad integration provided by a wide-ranging distribution and sales network. (...) During the year, the Russian business unit further strengthened this organisational structure with the opening of 14 brand shops to the existing network, which now totals 120 shops" (Marazzi Group 2008a, S. 25).

Since the delisting in July 2008, the market environment has changed significantly. The slowdown of all major Western economies is having a deeper impact than expected on the building material segment. However, Marazzi, due to its market-leading position and strong geographic diversification, remains well-positioned to consolidate its leadership and has managed to outperform its competitors and increase its share in all its key markets. The comparison with branch data shows that Marazzis success was supported through a slowly growing national market.

³⁷ A temporary dip was connected to the startup of a new factory in Malino: "the share of products produced at the new Malino factory doubled, which currently has only two production lines operating compared to the 4 programmed which is the optimal capacity level and therefore the proportion of overheads per unit produced is temporarily higher than target levels" (Marazzi Group 2008a, p. 25).

Marazzi Group: Performance of the Business Units (€ millions)

		2005	%	2006	%	2007	%
Italy	Revenues	479.8	53.1	504.5	52.3	516.8	52.5
	EBITDA	81.2	50.8	82.7	46.0	84.0	48.2
	EBITDA %	16.9%		16.4%		16.3%	
USA	Revenues	175.1	19.4	183.2	19.0	162.0	16.5
	EBITDA	33.9	21.2	38.2	21.3	30.1	17.3
	EBITDA %	19.4%		20.9%		18.6%	
France	Revenues	87.6	9.7	88.9	9.2	83.3	8.5
	EBITDA	4.0%	2.5	4.2	2.3	1.9	1.1
	EBITDA %	4.6%		4.7%		2.3%	
Spain	Revenues	82.3	9.1	86.3	8.9	94.2	9.6
	EBITDA	9.5	5.9	13.9	7.7	12.4	7.1
	EBITDA %	11.5%		16.1%		13.2%	
Russia	Revenues	78.4	8.7	101.3	10.5	127.7	13.0
	EBITDA	31.1	19.5	40.6	22.6	46.0	26.4
	EBITDA %	39.7%		40.1%		36.0%	
TOTAL	Revenues	903.2	100.0	964.1	100.0	984.0	100.0
	EBITDA	159.7	100.0	179.6	100.0	174.3	100.0
	EBITDA %	17.7%		18.6%		17.7%	

Source: Marazzi Group, as of 31 December 2007

Italy – Manufacture of other non-metallic mineral products

	2002	2003	2004	2005	2006
Enterprises	27,257	26,872	26,500	26,237	25,921
Turnover in € mio.	38,306	38,780	39,541	41,543	43,613
Employees	249,582	251,708	249,454	248,484	245,293

Source: Eurostat

6.8 The reorganisation of the company

In the case of Marazzi, the most evident consequence of the entrance of private equity funds in the ownership of the company was the reorganization of the organizational and managerial structure of the company, which was desired and supported by the employer:

*“The risk of family companies is that the leader often decides on 'gut feelings'. Up to a certain point it also has its positive aspect, but then, when the company grows, you can no longer allow it. A development model is needed. The targets that we set now are much more important than those we can reach at once by serious evaluation criteria are needed and the organization and the controls must be impeccable”.*³⁸

The reorganization of the company was conducted along two directions: the “managerialization” of the structure and the adoption of principles and organs of corporate governance in view of the Marazzi quotation.

³⁸ Filippo Marazzi, quoted in Pecoraro (2008), p. 70.

6.9 The “managerialization” of the company

At the end of 2004, when the private equity funds invested in the company, Marazzi was already a multinational leader in the sector with a strong presence in the United States. Nonetheless the organization of the company is still traditional, i.e. very centralized like the typical family companies along functional lines:

“There was the classical hierarchy with a delegated administrator, a general director and then other managers: It was a model that worked to create the group spirit, but by then the time had arrived for change, because the group had already grown large and the markets in which Marazzi worked were very diverse from each other, and therefore the business model to be adopted needed to be different”³⁹

The choice was to modify the organizational structure of the group from functional to one based on five business units based on geographic areas: Italy, France, Spain, USA and Russia. Each Unit is structured according to the characteristics of its geographic area and has its own staff functions (including research and development and marketing), production plants and sales organisation. Each Business Unit is managed by a country manager responsible for managing production and distribution activities in each country. The country manager reports to the group management and liaises with the other business units. China, an area where Marazzi wanted increase to their presence, presented peculiar problems that prevented the exact reproduction of the strategy followed in other countries. Instead, a corporate development division was created, with a director dedicated to the development of distribution in the area.⁴⁰

Accompanying the redefinition of the organization structure was the formalization of responsibilities and the delegation of authority of the various levels and bodies, “clarifying” (interview) the typical informality of a family company which, beyond its already multinational dimensions, continued to be a significant characteristic of the organization. From this perspective the organizational restructuring aimed at reinforcing the management team, with two delegated administrators supporting the leader (one for production, the other for finance) and new managerial figures to reinforce the functions of the staff in various areas, in particular:

- ☐ CFO
- ☐ Management Control
- ☐ Human Resources Manager
- ☐ Strategic Marketing Manager
- ☐ Business Development Manager
- ☐ Procurement Manager
- ☐ Supply Chain Manager

Lastly, since 2005, incentive mechanisms have been introduced for management in the form of:

- ☐ stock options plans for directors (up to a maximum of 4.1% of the capital)
- ☐ management by objective (MBO), which includes another 400 employees.

In 2006 the beneficiaries of the stock option plan went from 51 (2005) to 76 administrators and employees (directors, executives and high level management (Marazzi Group 2007: 46). There is no public information available for the following years.

³⁹ Paolo Colonna (Permira) quoted in Pecoraro (2008), p. 73.

⁴⁰ At the same time as the internal reorganization, the entrance of the PE funds was also followed by a rationalization of the group structure with the fusion, in 2005, of five Italian operational companies, all entirely owned (Ceramiche Ragno S.p.A., Ceramica Star S.P.A., Ramacolor S.p.A., 1-T One Tile S.p.A. and Ceramiche Finalesi S.p.A.) in the new group leader Marazzi Group S.p.A., with the objective of achieving significant cost savings and the consequent increase in profit margins and operational efficiency.

6.10 Corporate governance

For the purpose of bringing the company to the stock market, starting in 2005 a new *corporate governance* structure was introduced, characterized in particular by:

- a Board of Directors with a majority of non-executive directors;
- the presence of independent directors (including nationally renowned university professors);
- the introduction of a "Lead Independent Director";
- the constitution of a compensation committee and a control committee.

These elements of *corporate governance* were maintained even after the delisting.

6.11 Industrial relations

Present in Marazzi are trade unions from all of the three largest union confederations (CGIL, CISL, UIL) with a predominance of CISL. The results of the last RSU elections for company union representation (in 2007) were: 14 CISL delegates, 4 CGIL delegates and 1 UIL delegate).

The first European Work Council (EWC) agreement, which dates back to 1996, was renewed once in 2002, with an expiration period of three years (2005 and 2008). Along with the Italian unions the Spanish UGT was also a signatory to the agreement. The French unions are represented in the CAE, but didn't sign the accord. The EWC is composed of 14 members (1 representative per country + 1 representative for each union that signed), with an executive committee restricted to 8 members. The EWC accord doesn't present particularly significant aspects in comparison with other EWC agreements (European Foundation 2006).

Industrial relations at Marazzi have always been characterized by a cooperative style and direct relationships internally even with the CEO. When the PE investment was announced in 2004, "what we've emphasized and then obtained was the maintenance of industrial relations as in the past. And that's how it's been".⁴¹

Emerging from the interviews is that, on a personal level, nothing has changed with respect to family owners (Filippo Marazzi), while a certain change in the relationship with management is noted. The progressive "managerialization" of the company, with the additions suggested or wanted by the PE funds, has brought the substitution of figures key to the personnel function, which at the time were judged to be positive.

Interviews with trade unions also confirmed that no major restructuring processes took place, at least as far as the Italian plants are concerned. Factories were modernised during recent years, but this was considered part of a normal process and did not have a major impact on employment. Currently Marazzi has taken recourse to the Earnings Redundancy Fund (CIG), but this must be seen in the context of the strong economic crisis following the financial crisis. One should also keep in mind that two markets, the United States and Spain, in which Marazzi holds considerable shares were hit particularly hard by the housing crisis.

On the industrial relations level, the Funds represent more than an "invisible leader". The RSUs within the company, and the unions on the outside, don't have direct relationships with them but their influence increases in a crisis phase such as the current one. Information regarding the investment policies of the last few months is contradictory. On one side management emphasizes how, notwithstanding the difficulty of context, the company could have planned the enormous investments for the three years 2008-10. The same CISL representative states that the investments anticipated for autumn 2009, in the course of the negotiations on the renewal of the company contract, would have

⁴¹ Interview with trade union representative.

been planned in March 2009. According to the CGIL, however, the investments promised for the Italian factories would have been frozen.

The investments could have served to complete certain important operational changes in Italy, in particular the technological modernization of the most obsolete systems and the doubling of capacity of the Sassuolo factory, which is dedicated to large size products.

6.12 Summary: lessons to be learned from this case study

The Marazzi Group seems to be a “virtuous case” showing a positive economic outcome after the investment of PE, at least until early 2008. The private equity funds enabled the already internationally active company to continue its course of expansion and consolidation. In particular, the entry of Permira and Private Equity Partners is closely linked with the strategic investment on the Russian market which has been rather successful in the last years.

What are the principal reasons for this success story? Three aspects seem evident:

The first factor is the role of the Marazzi leader, who consciously chooses the private equity option to grow and be quoted, chooses among the private equity funds those which have not only a financial strategy but industrial as well and, finally, staffs the operational helm together with the funds themselves, but in a majority position, with clear industrial objectives for medium- and long-term growth.

The second reason is the characteristics of the company, a market and technological leader in the sector and with strong features of a family company. It was economically and industrially healthy but still with a traditional organizational structure that showed strong potential for further growth, making it attractive to private equity funds.

Tightly connected to the two previous aspects is finally and thirdly the peculiarity of the Marazzi operation conducted without using debt for the acquisition of a part of the share capital of the company on the part of the funds. This allows for the use of cash flow to finance enormous investments over three year periods and with an eye to the medium/long term.

The quote from Filippo Marazzi reported in the first part of this study also confirms an approach that is distinguished from a “locust” approach denounced many times as to the operations of private equity, which considers private equity to be an industrial business, not just financial.

On the other hand, the limits inherent in a case study don’t allow for the verification of how much this strategy is actually characteristic of the two funds, Permira and Private Equity Partners, or contingent or connected to the first two aspects considered. On the part of Permira Italia other analogous operations are known, with less positive economic results.

Finally, the analysis of the Marazzi case has to stop in 2007, since it is not possible to evaluate the company's current situation. As is seen, since the delisting of Marazzi, the financial data for 2008 and 2009 are not publicly available. Also in light of the financial crisis, the question of debts and liquidity of the company remain open. Mediobanca supported the delisting and the Voluntary Public Tender Offer of Fintiles with an additional credit of €285 million. The deal resulted in a doubling of Marazzi’s debts to € 550 million. The operation didn’t go by without comments in the business press:

“(…) with this upheaval, the group doubled its debt, bringing it to 550 million Euros, without adding anything to the factories or to the sales network. Not a single euro of risk capital enters the company in support of the investments, which, however, are only slightly larger than those already announced. Besides, an increase in capital today wouldn’t be necessary: the Marazzi Group generates enough cash and has enough lines of credit to carry out its industrial development plans. The operation seems to serve above all to liquidate a second fraction of the participation of the Marazzi family, which this time brings home

almost about 220 million, in part selling shares and in part indebting the company. The first fraction was surrendered in autumn 2004 to the Permira Luxembourg funds for 172 million with immediate collection and reevaluation. Permira then resold in February 2006 earning almost 155 million in the 12 months. In this second turn, Permira bet on the recovery of the value of Marazzi both for the effect of debt reduction, favored by fiscal saving on payable interest, as well as, and further still, for the effect of the recovery of construction that will arrive sooner later. At that point, Permira can exit the scene. Hopefully, but it won't be the only avenue, through a second exchange of stock shares".⁴²

Early in 2009 the management agreed with the unions, in the context of negotiations over the new collective agreement, to launch further investments for modernisation of the factories in Italy. However, these investments have apparently been suspended, allegedly on the initiative of the private equity funds.

7 Dinosol/Spain: A case study of a PE investment

7.1 Overview of PE, HF and SWF investments in Spain

PE is a form of investment that has existed in Spain since 1972, when it first became regulated. Since then some 4,655 companies have turned to this form of venture capital as a means of finance. PE activity in Spain is somewhat higher than in Italy and roughly at the level of Germany relative to GDP. Of the six countries under study the relative proportion of PE investment in the expansion stage has been the highest, accounting for two thirds of activity in 2003. Buyout activity has increased significantly over the period, growing from about one fourth to roughly two thirds of investment activity between 2003 and 2007.

The Association of Venture Capital Companies (Asociación de Entidades de Capital Riesgo, ASCRI) says that from the figures from 2007 the year can be judged as excellent for venture capital and for PE. Funds raised nudged € 5.2 billion € and investment came in at € 4.33 billion. This formed the backdrop for a very good year 2008, although the financial crisis forced a complicated year-end.

The scenario changed from the summer of 2008 when the financial bubble burst and the liquidity crisis in the lending markets came along. Although the branch showed an acceptable performance in 2008, it is however clear that the golden years of this sort of activity are history and it is admitted that returns are set to fall to half their levels, from 25% to 12% on average. According to the chairman of Altamar PE, a leading venture capital fund it can be stated: 'Financial engineering has disappeared. Investment and disinvestment time horizons will go back to being five or six years and not two or three as they have been up to now, with greater value in management'.

Fund-raising in 2007 hit a new record at € 5.24 billion, the figure up 34% on that for 2006. Pension funds from abroad made the biggest contribution at 24%, above the slice from banking, which came in at 23%. The share of domestic investors, however, shows a growing trend compared to the European component. In total 48% of investment comes from domestic investors and 28% from European countries. The US put in 20% of total investment in 2007.

The firms with the strongest presence in Spain are: Candover, Carlyle, Doughty Hanson, Cinven, Apax and 3i. The number of transactions closed 2007 was 840, compared with 765 the previous year. 85.6% of transactions involved investments of over € 10 million. The trend points to a rising volume.

The sector composition is very similar to the profile for the other EU countries, with a powerful presence from the traditional sectors, with the following leading the way: other

⁴² "Marazzi, when the industry makes finance and the funds rich", by Massimo Muchetti, Il Corriere della Sera, May 24 2008.

services (20%); hotels, catering and leisure (20%); energy and natural resources (10%); medical and health (10%); communications (9%); consumer products (6%).

Recent developments of PE investments in Spain

The situation on the PE Market is moving fast. 2008 still seems to be tracing a 'traditional' trend, similar in structure to previous years and showing a hangover of inertia with respect to 2007, though in the words of an expert in finance the PE *modus operandi* has, *de facto*, all but disappeared.

Certain recent movements in Spain shed light on the sensitivity of this sector to the crisis and, more specifically, to the problems that some investee companies can face. The sector is not immune to the phenomenon of restructures and job losses. For example, 3i, a pan-European firm that owns companies in Spain such as frozen-foods group La Sirena or funerals company Mémora, has set in train a downsizing programme for 15% of its staff (100 out of 660 workers), having raised its provisions and marked down the value of its portfolio of companies in which it has investments.

More than in investing, the present activity of these companies now focuses on heading off impairment of their investee companies. In 2008 the sector giants have tip-toed through Spain. The number of transactions over € 100 million was merely symbolic: scarcely a dozen, as compared with 2007, when there was record investment of € 4.33 billion. There are larger companies such as CVC, Doughty Hanson, Carlyle, Permira or Cinven which have not made an appearance all year. The figures for the year not having been closed off, two thirds of transactions are in expanding companies and only one third is in leveraged deals, compared to 50% the previous year.

The number of workers at companies invested in by venture capital and PE companies in Spain is some 387,000. The average number of employees at invested companies is 198, this showing an upward trend as investee companies in 2007 alone raised average staff levels to 222 workers.

Identified HF equity positions at the end of 2008 are modest, accounting for less than 1% of shares outstanding in all of the top 20 HF equity positions by value. All of the top 20 equity positions in companies listed in Spain were accounted for by the Norges Bank.

7.2 Dinosol – Private Equity investment after economic crisis at Ahold

Introduction: why the case was selected

In December 2004 Permira, one of the largest PE companies in Europe, bought the Spanish supermarket chain Dinosol from the Royal Ahold Group. There are a number of reasons for select this case:

It is a large investment by one of Europe's most important PE companies in a food market which is characterized by fast restructuring processes in Europe. Investments by PE in retail companies like Dinosol or Alliance Boots are very characteristic for the market development in the last 10 years.

The typical financial re-engineering used by PE can also be seen in the Dinosol case due to a lack of restructuring analyses in the retail distribution sector. The restructuring processes that are analysed more commonly are in industrial companies. In general, although restructuring processes usually imply a large number of job losses, this is a sector that is rarely known and does not regularly appear in media headlines.

The outcome of the restructuring process can be seen as successful. The case shows that it is possible to manage restructuring by moving away from the oft-cited protocols used in cases of acquisition by a PE fund: acquisition and immediate adjustment of labour to rationalise the undertaking acquired. In the case of Dinosol, new management and trade unions have designed an Employment Plan which decreases the practical effect that the rationalisation process has on the social part of the undertaking. The Employment Plan has managed to maintain practically all employment and has been carried out fully, with such success that it has been extended due to its versatility to articulate industrial relations in a group dominated by the dispersion of its assets throughout the country. The result seems optimal and the group has been reorganised. It now aspires to improve its position within the sector, having dispersed of obsolete assets. Employment has not suffered significant losses and the mechanism of industrial relations

has been strengthened, with an increase in membership of the most representative trade unions as a response to management of the crisis situation.

The restructuring of DinoSol is to be seen within the context of two driving forces. (1) Permira has acquired ownership of the group based on the freedom of action for any stakeholder in a rationalisation process of the activity on a global market. To this, we must add the absolute freedom in the movement of capital that provides the cash flow required to undertake the purchase. However, the solution to the subsequent restructuring process is in keeping with an almost family-scale conflict-solving process. (2) It must be highlighted that Ahold was a business group renowned for its commitment to a culture that is respectful of the rights of both sides of industry, in favour of negotiation and agreement. This was, however, something which did not prevent fraud. Permira is a risk capital group that is not particularly known for commitment beyond obtaining the greatest profits for their funding shareholders. However, Permira has not objected to the design and execution of the Employment Plan on condition that it allowed rationalisation of the group, thus agreeing with the point of view sustained by trade unions, management and experts.

7.3 Profile of the company and the financial investors⁴³

The DinoSol Supermercados Group

The DinoSol group includes the following undertakings: Supersol, Hiperdino, Hipersol, Dino, Netto, Cashdiplo within the sector of retail trade. Employment has fluctuated over the years, mainly upwards, and at the present time, Dinosol has a staff of around 11,000 workers.

The group's establishments are located in Spain (Madrid, Barcelona, Andalusia, Castilla-la-Mancha, Murcia, Canary Islands). They are widely present across the country, except in the north and increasingly less in Catalonia.

The company currently occupies the seventh position in the rank of retail trade undertakings in Spain. This is the same position held by the group when it was acquired by the Permira investment fund in the year 2005. This group is not alien to movements in the sector; it is close to the profitability improvement averages in the sector although its relative position remains unchanged. Hence, even though the group has improved its profitability ratios, in general terms, with regard to warehousing surface and points of sale, it improves in line with competing groups.

In 2007, the group was in the view of some analysts specialising in buying and selling companies. Everything indicates that this was due to the consequences of the Eroski food group operation to acquire Caprabo, which gave rise to comments in the specialised press.

The group has more recently been guided by a strategy to consolidate its position, based on the strength of the group's core. Future enforcement of the Law to Deregulate Trade will make competition fiercer and will make consolidated business areas more vulnerable, for instance in the Canary Islands. For this reason, it is to be noted that one of latest and greatest investments in 2009 has been carried out in Adeje (Tenerife) with the start up of a new emblematic centre.

Permira Investment Group

Permira is a European private equity firm with a global reach. Permira funds, raised from pension funds and other institutions, make long-term investments in companies

⁴³ The case study is based on interviews and material provided by different stakeholders: management representatives (Head of Human Resources and Head of Finance, Administration Director Public Banking, Risk Capital Operations Director Public Banking).

with the ambition of transforming their performance and driving sustainable growth. Permira was founded in 1985 and has made over 190 private equity investments. To-day, the firm's teams advise funds with a total committed capital of approximately € 20 billion (\$ 28 billion).

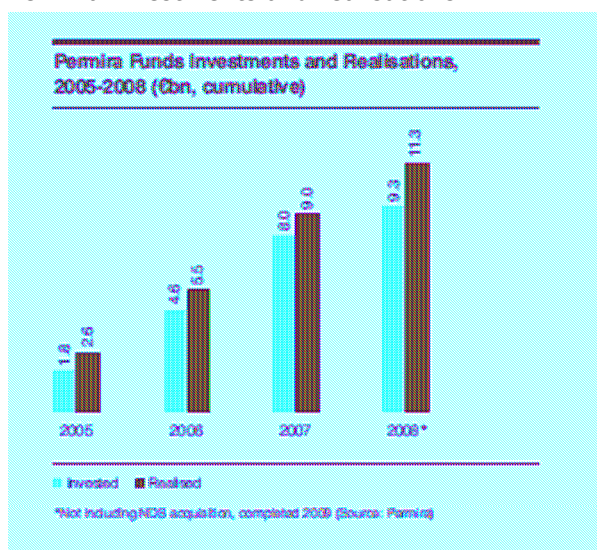
Permira Group opened its offices in Madrid in 2004 as a result of the Pan-European strategy of the fund located in the UK. The number of managers that make up the staff in Madrid is six, with different technical responsibilities and supported by the resources that the group supposedly has in its centres and global networks.

Permira declares its preference for certain types of operations: financial acquisitions; buy-out, buy-ins; public to private transactions, refloating undertakings. They seek the following: de-investment in non-principal assets; development of family businesses; promotion of the organic growth of businesses; operational improvement of low-profitability assets; consolidation in the sectors by means of strategic acquisitions.

All of these operations imply investments in excess of € 500 million. As may be seen, the logic behind the group has focussed on the macro perspective of the economic activity, over which the profits of shareholders or participants in the funds practically rule the development of the general business strategy.

Permira operates mainly in the chemical, industrial, telecommunications, financial services, health, and trading sectors. Permira classifies its investment strategy in this way in its official statements.

Permira investments and realisations



Source: Annual Report 2008, Permira Group, p. 14

Since 1985, Permira Funds have made over 190 investments. The fund has consistently outperformed the stock market over past 20 years delivering consistently strong return across economic cycles. Today the fund own over 20 companies around the world.'

To date, its maximum investment can be found in the acquisition of TDC (Denmark), a technology and communications company. This acquisition required an outlay of € 13.400 million in 2005. One of its latest acquisitions was in 2009 with the acquisition of NDS Group (UK), which is also a company in the communications technology sector, for € 2.461 million.

7.4 The acquisition process

The trigger for the sale by the Ahold group to Permira was directly linked to the former's US division's accounting fraud and the appearance of a void in business which had to be balanced with the sale of assets, amongst which was the group's section in Spain. Nev-

ertheless, the evidence suggests that Ahold's Spanish section was not in a state to hold on much longer, even without this blow. Ahold's US divisions accounting fraud shares had plummet from € 15 to € 2 on the day the fraud was known. When the US scandal started, the Spanish company was about to file for bankruptcy protection. The total size of the transaction was € 895 million.

The sale was preceded by several months wait during which several interested buyers appeared. Sagardoy Abogados, a law firm specialised in sales operations of undertakings, mediated as a consultant group in making the transaction official.

In December 2004, Permira Funds purchased 99.9949% of the Company's shares from Ahold through Company CMA S.a.r.l. In February 2005, the company name was changed to Dinosol Supermercados, S.L. The undertaking started a period of restructuring that lasted throughout 2005.

Situation of the company at the beginning of the transaction

DinoSol is amongst the top five groups in retail distribution in Spain as a result of Ahold's acquisitions. It has a distribution surface of 503,000 square metres, over 63% of which are dedicated to retail. According to official records of Permira, the group is in seventh place in the general rank of all its activities (retail, convenience stores and cash & carry). In the Canary Islands and extensive areas in southern Spain, the group is leader in both supermarkets and convenience stores (Netto).

Competition takes two forms. Firstly, it comes from other companies in the sector. In this sense, competition is solved by means of occupying strategic positions and developing price policies adjusted to the characteristics of surrounding population or potential demand. Secondly, competition between different undertakings specialised local stores on a micro level and on macro-sales in large surfaces. The supermarket, DinoSol is an example of this, placed between the corner shop and the large surface. The general opinion is that the sector, and not only the DinoSol chain, is setting and increasing its position to face both of these. Prices usually overcome micro-competition from corner shops. Proximity and human size defends it from mega-stores.

The future transposition of the European Directive on Services into Spanish legislation will entail a partial liberalisation of the legal requirements to open shopping centres, the authorisation of which depends on regional and local governments. This will give rise to a competition war that will come on top of the current price war, substantially modifying the current market situation.

Permira is known to have paid half of what Ahold paid a few years back for the Hip-lodiplo chain alone (€ 1.200 million) for all the capital (€ 600 million).

The new board of directors sets strategic direction. The new owners clearly state their intention of staying no more than five or six years, refloat the group, and sell it at a profit due to increased profitability. In doing so, the Fund Group is faithful to the workings of the PE investment model.

The restructuring process following the acquisition of DinoSol by the risk capital Permira Fund requires a broad view in order to understand its causes and establish a chain of reasons found in this process which will clarify its development. We must highlight that the retail trade sector is in general still undergoing a wave of transformation in the search of the ideal volume for each type of proposal. The determining, leading market position has not yet been found by any stakeholder in particular, although each group has been able to establish a stronghold, which in the case of DinoSol is found in its monopoly presence in the Canary Islands.

Strategy of Permira

Permira sees the acquisition of Dinosol as a 5 year acquisition, at the end of which it will be sold on or floated again on the market. Its approach to the management of the company is to set broad financial parameters and then to leave the rest to DinoSol executives, most of whom are long-standing managers in the company. The aim is to invest in some new stores, to close others, and to put more resources into technology and organisation.

Permira has undertaken a viability analysis and considers the closing down of stores and the disappearance of duplicate functions unquestionable. This involves the closing down and / or sale of 60 stores and the disappearance of approximately 900 jobs. This also coincides with the appreciations made by the former board of directors and with trade union estimates.

A top management team has been appointed from the managing staff in the former undertaking and entrusted to develop a model to approximate the profitability rates expected by the new ownership. The fund managers are specialists in risk capital, in taking advantage of opportunities, and designing profitability programmes for potential situations. The purchasing group is, therefore, an expert in maximising profit, not in the retail trade, even though there is a trend towards certain specialisation which is appreciated in their choice of financial experts in the field of retail trade placed to direct this project. Their expert knowledge has been consolidated by hiring acknowledged companies in accounting (Ernst & Young) and legal coverage of sales operations (Sagardoy Abogados). Contracting of expertise in these fields does not seem to be determining in the restructuring process but defines trends in the implementation of external 'expertise' other than the stakeholders themselves.

A top manager in the group has commented, "Permira are quite tight with money." Typical for a PE case is the de-investment process which took place some short time after the take-over took place. To recoup some of the invested money, Permira forced the Dinosol management to commence a sell and lease back program in January 2005. This frees up cash for Permira but affected the balance sheets. In 2006 Dinosol took on additional debt and in February 2007 more money was taken out of the company by paying a € 488 million dividend to Permira. There have been some further smaller acquisitions by Permira in the retail sector in Spain.

7.5 Consequences for core business and for employment

The acquisition process followed the usual pattern of PE funds: that is, to obtain the ownership of a company, not accessing an enlargement of capital as is usually the case in risk capital investments. This constitutes a difference because in the enlargement of capital an alliance is reached between former and new owners of the company. In private operations, such as this, this is not the case. A new ownership substitutes former ownership, and has its own strategy.

In the Permira-DinoSol case, the strategy seems to focus on assessing resources and strengthening the trade strategy. The strategy seems to indicate a line of improvement in the consolidated business model, which is the basis of the retail trade sector.

The sector has been in a very similar situation in the last few years and DinoSol is highly adapted to the structure in which retail trade operates. The model implemented by the undertaking 'Mercadona', the most successful formula in the supermarkets sector, continues to project a pattern that is considered to be optimum in the market. The only event to be highlighted is the recent sale of all its centres located in Catalonia (with the loss of 1.000 jobs), where the brand found strong resistance and its presence was not a determining factor in the group's position.

However, short-term movements continue to take place in the form of buying and selling areas of activity, with the annexation of small chains or territorial areas of activity. For instance, Dinosol has sold part of its assets in the province of Avila to the re-established Árbol group, which after years of instability has been acquired by a group of savings banks from Castilla-León. This seems to be the dominant trend: if a good opportunity arises to buy or sell, then it is carried out; however, these movements are not related to the organisation or development of activity in the sector. They are specific, not structural actions. It is not strategy, but more business opportunity.

Amongst new developments, the future application of a new law transposing the European Directive on services may be highlighted, as it will introduce greater deregulation with regard to eliminating legal requirements to open new establishments. Licences to open new establishments are currently a joint responsibility between regional governments and town councils, who grant permissions. The Directive will eliminate local restrictions, leaving exclusive competence in granting licences to the national or regional governments which will have no other limitations than those arising from the environmental impact that a new centre may have, or its effects in the context of cultural heritage.

It can be concluded that Permira has increased its interest in the retail trade sector with successive buy-out investments: the acquisition of a majority share in two institutions with a long tradition in Spanish territory. (a) On the one hand, it has acquired Cortefiel, a company in clothing and fashion, a prestigious mid-level brand specialised in 'classy' prêt-à-porter. (b) It has also entered the home-delivery food segment with the acquisition of Telepizza, dedicated to the preparation and distribution of readymade food, a company with great potential as it is one of the few companies operating in the national market which has managed to open the doors of Spanish homes traditionally reluctant to this. However, retailing is not an easy sector in Spain. Quite the opposite: CVC, the other investment fund present in the sector, which was co-owner of the Árbol group, has disinvested by selling the group to the savings banks in Castilla-León.

The overall strategy of Permira in this sector remains unclear. One can point out that the assessment process of 'companies' which can be acquired is very complex, generating a very specific 'expertise' which motivates Fund managers to continue working in sectors that start to dominate after assessment of previous cases. However, this is only a hypothesis that can not be contrasted, since what seems to dominate the interest of the investment group is opportunity, that an average company appears in the horizon that is cheap, may be improved, has liquid assets on the one hand, and access or resources for debt, on the other.

7.6 Economic development

The concentration process undertaken in the last few years in Europe is a determining feature in the retail trade sector. In Spain, this process existing at the origin of the Dinosol group is similar to the process followed by other retail groups such as Mercadona and Caprabo which are the competitive reference point for Dinosol.

The concentration process has followed a homogenous and linear pattern in all cases. Purchase and acquisitions of groups present in strategic retail trade areas and annexation of small, local family-enterprise establishments. This strategic push, guided towards obtaining volume, is sometimes reinforced by opening newly created centres. Nevertheless, new centres do not amount to 10% of available retail space in any of the important groups in the sector.

As with other groups in the retail sector, Dinosol is the result of a process of acquisitions, started in the mid-90s and carried to its logical conclusion by prior ownership, Ahold. The acquisitions' process is sustained on the basis of a double logic: (a) adapta-

tion to social and demographic changes and (b) reaching a strong position in negotiation with suppliers.

Changing lifestyles with radical transformations in social, family and urban geography are the origin of alterations in purchasing cultures, forcing companies to make commercial proposals which adapt to the models resulting from the process of social transformation.

However, even though adaptation to social changes is a current issue in group formation in the retail trade, reaching a dominant position in negotiation with suppliers stands out as the first economic factor underlying the concentration process. Retail trade has a profit margin of approximately 3%. This margin is sufficiently small for price and sales return negotiation on aggregate purchase to become a determining factor in business success. Reaching an advantage position for price negotiation and methods of payment has become the focus point in acquisition strategies in the last few years for retail groups in Spain.

Investment policy

The group's investments are dominated by policies which are not generic in all undertakings in the sector: defending the position and maintaining sales.

The former is achieved by improving premises in favourable locations and the development of logistics and selective warehousing centres, especially in Andalusia and in the Canary Islands, where the group is mainly located. Investments in these segments are compensated with the sale of less favourable territories. The sale of assets in Catalonia and parts of Castilla-León are a proof of this policy of investing only in fertile territory.

Investments to curtail competition are focused on maintaining the price war that is rife in the sector, the result of a fall in income which the financial crisis has caused. Up to 90 low-cost products have been placed on the shelf, with prices up to 15% below the private labels they must compete with.

The strengthening of the group's marketing has been significant, with a clear commitment to high-profile communication and advertising. This line of investment has been stimulated by the investment management, Permira. However, it would be true to say that all retail groups have similar lines of investment. If there is something to highlight in the investment management carried out by Permira, it is the rigorous assessment of all resources invested. The 'rigorous' analysis of investment has moved from the fund's management (Permira) to the group's management (DinoSol) through a sort of transfer of investment assessment techniques.

The other large space for investment can be found in technological development. Information and Communication Technologies (ICT) are present as transversal technologies, with a greater potential for use in management and administration tasks than in transforming the main or auxiliary processes in the retail trade.

Only the attempts to implement software to integrate stock management and stock replacement in stores with automatic stocking systems can be highlighted with regard to logistic systems applied to the sector, together with the first attempts at robotisation of tills with regard to hardware and equipment development. Several models for product recognition are appearing with difficulties to substitute tills, where a significant proportion of employment in the sector resides. This is therefore an emerging technology that will have a certain impact.

Both lines of innovation will undoubtedly be developed and will probably be integrated in a techno-methodology to automate payment management and the management of replacement orders. This will be in the near future, but will not apparently cause a radical transformation in the activity or in employment. Supermercados Dinosol is no exception.

The group remains on the alert, but it does not appear that technological advances will determine its future.

Market performance

The group undertakes its activity through the following names: (1) Supersol and Dino (in the Canary Islands) under supermarket format; (2) Hipersol and Hiperdino under hypermarket format; (3) Netto (in the Canary Islands) specialised stores for tourists; (4) CashDiplo, wholesale for food stores and restaurants.

It uses and works with the main national and international manufacturers and suppliers of food and other products. Likewise, it keeps business relations with specialised local suppliers in each region. This is especially so in Canary Islands.

DinoSol is the seventh largest undertakings with largest turnovers in retail food in Spain and holds the top spot in the Canary Islands. Turnover in 2008 amounted to € 1.669 million and an EBITDA of 69.2 MM with accounting criteria comparable to the previous year.

The upward trend for the next three years is expected to continue and an excess of € 1.800 million in sales is expected. However, the general economic situation in Spain was characterized by a stable positive growth. The growth of turnover in the retail sector was even more dynamic between 2002 and 2006 as the following tabel shows.

Spain - Economic indicators

	2003	2004	2005	2006	2007	2008
Real GDP growth rate	3.1	3.3	3.6	3.9	3.7	1.2
Employment rate in %	59.8	61.1	63.3	64.8	65.6	64.3
Unemployment rate in %	11.1	10.6	9.2	8.5	8.3	11.3

Source: Eurostat

Spain – Retail sale in non-specialized stores

	2002	2003	2004	2005	2006
Enterprise	39,958	35,373	33,780	33,707	32,886
Turnover in € mio.	60,936	63,113	68,174	72,553	77,408
Employees	421,127	421,842	438,385	461,672	461,816

Source: Eurostat

7.7 Development of employment

The restructuring process implied the closing down of stores and transformation of offices resulting in 800 job losses for which the agreed Employment Plan implements one solution or another. Below is the summary of the actions under the Plan. The number of workers affected in stores is 502. They have been dealt with in the following ways: subrogation 167; relocation with same conditions 120; relocation with modifications 31; deferred relocation 26; 35- or 40-days compensation 119; termination of employment 39. The number of workers in offices over the same period is 138 and they have been dealt with in this way: relocation 64; 35- or 40-days compensation 74.

There are very small numbers of personal solutions or end of contracts agreed unilaterally by workers individually. We must take into consideration that some professional specialities in the retail sector are highly sought professional qualifications given the scarcity of professionals in the areas of meat and fish. Dinosol has a school for human

resources' development of these profiles; similarly in other undertakings of the competition. Mercadona's professional school is well regarded. Nevertheless, the existence of these schools is insufficient to fill the market with the qualifications demanded by a growing sector without the acknowledgment or provision of regulated professional training.

This is perhaps one reason why the rationalisation of staff under the Plan has not been very aggressive. Nor has it been a traumatic experience in sectoral or territorial terms. The largest conflict in employees' situations, their expectations, and the solution adopted by the Plan has appeared amongst office administration staff, for which a functional polyvalence criterion has been implemented and has been reconverted into staff in tills and stock replacement.

The Plan is still in force. But employment volume is stable since the end of the Employment Plan was implemented. 1,000 jobs have been lost in Catalonia, which have been transferred as subrogation to the company acquiring the assets in those regions.

An agreement has been reached between trade unions and the company to modify the stimulus and motivation policy through a General Incentives System (2009). Summarily, the agreement tries to rationalise a policy to control absenteeism and general reward towards a policy focused strongly on acknowledging merit, linking criteria related to achievement, increase in profitability and increase in productivity with collective and individual rewards (store, line, department and person).

There is policy aimed to promote open-ended contracts, reaching 73% of all contracts. 75% of all employees work full-time.

The business training/culture project, called 'Friendly staff' must be highlighted. Implemented in 32 stores, it has increased qualification levels of workers involved and the loyalty level of consumers.

There is a plan to welcome new employees. The 'welcome tutor' project is a training process to generate tutors in all stores. 1,374 training courses have been undertaken from 2004.

In conclusion on Dinosol, it has a staff that amounts to 11,000 workers in 2009 having the following characteristics. 60% are women and 10% are over 50 years old. 80% of the staff has a low skill level; 15% are at middle-to-high qualification level; and only 5% have university education. The number of employees affected by restructuring is 900, from different levels, roles and qualifications. Out of these, 60% are women and 10% are over 50 years old.

In the case of Permira itself, employment is limited to a small number of technical staff specialised in buying and selling assets, with broad training in financial management and legal regulations. Financial management and commercial law are the basis for their qualification which becomes progressively robust as they become immerse in successive acquisition processes.

This results in the specialisation of the technical staff in the fund's management unit, which in this case is reinforced by the incorporation of a specialist in retail activity. Management funds incorporate and develop a tremendous amount of 'intelligence' in terms of modernisation and improvement of qualification. However, this is not reflected in the volume of employment. Nevertheless, outsourcing or purchase of highly specialised services is a strategy that is part of the fund's potential.

7.8 Consequences for industrial relations

The investment group is not involved directly in the group's management, except in financial assessment. In particular, it is not involved in industrial relations. It places one or more persons (depending on the case) in the boards of company, who act as notary

publics of the general behaviour of management in these fields. It seems that the business approach is designed in a single annual meeting (viz. board of directors) where the objectives and the framework are set. Policies affecting industrial relations as a whole are considered to be second-order management lines derived from the macro charts in which the investment group intervene directly.

Summarily, it could be said that the investment group sets the business lines and drafts the scenarios for profitability. It supports the strengthening of assets from its economic-financial management platform. From there, the development of specific policies is responsibility of group DinoSol's own management. The industrial relations policy, important given the volume of employment and how widespread it is, is channelled through open dialogue formulae with social partners.

Execution of the plan has tended to strengthen the presence and legitimacy of the most representative trade unions (Unión General Trabajadores and Comisiones Obreras), which have acted in coordination. Their presence has been valued highly and the number of members has increased due to how reorganisation has been handled.

The Employment Plan

The Employment Plan was an action agreed by the management and worker's representatives with the intention of developing a restructuring process to limit the, apparently unavoidable, more traumatic effects of implementing the legal form or ERP.

The plan involves seven measures. The most significant issues of each of the seven measures are highlighted below.

- ☐ Favourable instrumentation: Implies the acceptance of a legal treatment that assumes positive discrimination towards employees de facto.
- ☐ Direct relocation: Conditions are established which will develop direct relocation in the undertaking and setting criteria of functional and / or geographical mobility. Compensation is also established for excessive mobility that may take place in specific cases.
- ☐ Deferred relocation: Measures are established for deferred relocation to third-party institutions. A mechanism has been established – so-called relocating guarantee deposit – to neutralise the inconveniences of the relocation period. The possibilities and situations for rejection and acceptance of relocation offers are defined.
- ☐ Compensation for direct redundancy: Implementation of settlements per employee in the case that the end of the relationship between employer and employee is solved.
- ☐ Compensation for alternative redundancy: Definition of alternative redundancy, implies the implementation of the following model: 35-day gross annual salary per year in service, with a maximum of 42 monthly salaries.
- ☐ Monitoring Committee: Number, composition and working statute of the monitoring committee formed by representatives of each of the undersigning parties (equal distribution, made up of 8 members).
- ☐ Validity: One year which has been extended.

Trade union representation

There are four trade unions with representation and membership in the group. Two main trade unions, Unión General de Trabajadores (UGT) and Comisiones Obreras (CC.OO). The Confederación General del Trabajo (CGT) is present in Andalusia. They comprise the set of trade union organisations pursuant to the pattern followed by collective bargaining at province level. The number of members amounts to 1,300 approximately; this is approximately 12% of all workers.

Spanish legislation does not promote the organisation of inter-centre works councils and, therefore, the industrial relations structure is articulated upon provincial works

councils. Collective agreement is undertaken on a provincial level. There is no collective agreement for the undertaking.

The special features of the restructuring model arisen from negotiation between the undertaking and trade unions have involved the creation of an organic unit which did not exist previously. A National Council that, similarly to inter-centre councils, has been set up with the single aim of designing, adjusting, negotiating and safeguarding the fulfilment of the Employment Plan.

It should be noted that the Council, which represents the stakeholders' interests, has no legal support. Its legitimacy comes from the agreement made in view of the restructuring promoted by the new ownership of the supermarket chain.

Areas of negotiation

The restructuring process deals with two areas; the closing down of stores (approximately 60) and the elimination of a certain number of jobs (approximately 800).

The forecasts made by the board of directors of the group, workers' representatives, and the formally independent auditing company all agree. There is also agreement in the analysis of the undertaking's situation and in the viability programme. The group and the employment generated within it will not be sustainable unless a restructuring process is faced to purge duplicities and obsolescence generated by past indiscriminate purchases.

In order to tackle the restructuring process, a joint committee has been created with 8 members, 4 representing the undertaking and 4 representing the workers (two members each of the most representative trade unions, UGT and CCOO). This is a national-scale committee and replicates a non-existent inter-centre works council. As stated earlier, this committee designs, monitors and legitimates the Employment Plan which is the document ruling the restructuring process as a whole.

The climate of industrial relations and social peace

Social conflict caused by restructuring has been channelled as it has been submitted to an agreed negotiating process at all times. This does not imply that there was no disagreement. Particularly controversial where complains from the CGT who accused the most representative trade unions of submitting in agreement with the board of directors. The most outstanding act was the invasion of a national council meeting. The groups gathered in the meeting were accused of a lack of commitment with the workers during this transgressor act, followed by the publishing of satirical posters and leaflets condemning the situation as they saw it.

At the initiative of the CGT and FTYCO unions, the services of experts in labour law were contracted to analyse the restructuring process in order to issue recommendations. The law firm in charge advised that the best formula was the one being negotiated in the council by the most representative trade unions. This ended in disputes between different workers' representatives.

Given that the undertaking's activity is widespread and split into units scattered across the country, the impact on employment induced in the value chain has been scarce and, hence, there has been no conflict.

Both the management at DinoSol and workers' representatives grant a significant weight to these social dialogue mechanisms with regard to the transfer of one property or another, in the limiting of core and collateral damages and in the minimisation of operational alterations that could have made the process fail or the brand disappear, as there are previous experiences of this happening in the sector (group El Árbol).

Hence, the mechanism for dialogue started by the Employment Plan, and which continues to be the tool to incorporate successive stages of negotiation and adaptation, was and continues to be a valuable cornerstone, a highly valued and acknowledged instrument.

7.9 Consequences for work organisation

Work organisation has not been altered by the investment group's entry. The only event worth highlighting is the re-occupation of part of the administrative staff, who have become cashiers. This is the most striking and complex event, since the change in productive objectives is significant but no change has taken place in terms of salary, working hours or other non-functional attributes. A group of 40 workers with administrative duties have started working as cashiers, in warehousing and stock replacement.

Dinosol has the typical supermarket chain system of organisation and work organisation in its stores, warehouses, and offices. There is nothing particular to remark in this respect.

7.10 Corporate and management elements of the acquired group

The top government body is the board of directors formed by a president, vice-president and five directors. Concentration of 99% of shares in Permira results in a homogenous board with a semi-operational nature. Their decisions go from strategy definition to design or validation of action policies.

The governance chain is articulated in one centralised General Directorate with specialists in each role: Purchases, Commercial, Logistics, Finance, Human Resources, Administration, with headquarters in Madrid. Under the direction of the Managing Director, this team extends its command in regional offices that replicate the functional roles at their level.

The design of action policies and their execution is the responsibility of the central body. Regional offices are in charge of developing and reporting on them and negotiating the peculiarities in implementing the lines of action in each of the territories. Responsibility is as concentrated as the group's government organisation. The regional offices' responsibility does not go beyond their capacity to manage minor details of the group's general policy.

It is therefore a strongly centralised organisation, perhaps in order to compensate for the extremely dispersed deployment of establishments; we have not been able to confirm this. We cannot state that this model is the product of a need or of a business culture anchored in hierarchical organisation and centralisation.

The operational monitoring activity follows the organisational structure of centres described in another section. There is a store or warehouse manager, depending on the type of establishment, section managers and shop assistants who share responsibilities in the fulfilment of operational objectives but who do not take part in decision-making.

Business Plan

The business plan envisages the following: on the one hand, reinforcing investments in the geographical areas where the group is in a leading position, especially Canary Islands; on the other, project the group's activity towards objectives that reinforce its position and improve profitability.

The following objectives may be highlighted. First of all, there are a set of objectives in broad areas: to strengthen loyalty programme and marketing policies; to win over new business by means of offers focussed on price, quality, and service; to increase income per square metre and improve profit margin; and to increase financial resources generated by the undertaking's business and cash flow management. There are then a set of

objectives related to rationalisation: to maintain the policy of store reforms and rationalisation of portfolio by means of transfer and closing down of establishments that are far from strategic positioning; to continue with the opening of new stores; and to rationalise logistics. Larger percentage of centralised products distributed to points of sale. Finally there are then a set of policies related to more operational matters which intersect with human resource management: to reduce expenses by cutting employment and improvement of operational and management processes; to develop of training and better service delivery.

The direction of change

Since the acquisition in 2005, the management team has remained unchanged. This team which was the promoter of the Employment Plan together with trade unions, is still involved in the direction and execution of the Plan, its extension and, especially, in the development of the Incentives Plan which is a central part of the Human Resources policy for 2008-2009.

DinoSol's direction has mainly focused on improving business profitability in a conventional way: improvement of surface/sales volume ratios, improvement of supply systems with a firm commitment to specialised warehousing centres and an increasing quality of suppliers. In this, it works as the sector as a whole.

How far strategies developed within the investment group have influenced decisions at Dinosal is unknown. The technical investment managers from Permira attend the Board of Directors meetings and they set their expectations. They do not have permanent and direct action in directing the group, nor do they intervene in the 'field' directing bodies.

The company's direction is committed to the group's development, which in a professional way is weaving a strategy for its consolidation. However, the possibility of being sold is present at every moment. Not only because the sale option is objectively possible at any time and for everyone, but especially because the owner, the investment group, is more open to making a profit as part of a business opportunity than other owners.

Hence, DinoSol's direction is under a double Sword of Damocles: the possibility of being sold at any moment and knowing that the owner is more prone to selling than other forms of ownership. This affects leadership and morale.

However, as this is an almost daily practice, the directions at the undertakings seem to have found a form of acceptance that does not damage their capacity for leadership or their management model, which, in any case, isn't too sophisticated. Whatever can be solved with money takes precedence over any other initiative. This turns DinoSol into an example, since the Employment Plan took precedence over the Employment Rationalisation Report, giving rise to a type of group heritage or conduct with regard to dealing with any policy affecting workers through dialogue.

7.11 Other known investments of the financial investor in the same branch

The investment group has carried out a number of small volume acquisitions guided to improve market share in some territories, especially in Andalusia and Canary Islands, and the sale of assets located in Catalonia. However, this is not due to a policy for expansion, but to consolidate its position.

A general strengthening of the investment group in its activity in the retail sector has more or less taken place. This strengthening does not imply direct investment in retail trade assets, as in the case of the group DinoSol, but in assets and undertakings on the periphery.

The group has acquired Cortefiel, a well positioned retail brand in the national clothes market, in 2006. Similarly, it has acquired Telepizza, a readymade food company, basi-

cally for home delivery. This is an important acquisition, since it is one of the few undertakings that has managed to open the doors of Spanish homes, traditionally reluctant to this in situ purchase behaviour from home. It has great potential through this open door channel. It has tried to acquire the group Aldeasa, which is the licensee to exploit airport shops in Spain. It presented a pitch to acquire the exploitation license, but lost the tender which was won by the Italian group Auto Grill.

Besides the profitability that may be obtained by improving these business exploits, it can not be stated that a general strategy exists on behalf of the investment group, which is present in many sectors. Even the executives at group DinoSol warn us about the possibility of being sold at any moment, and hence the bond between the investment group and the undertaking responds to a situational and undefined relationship.

The investment group's attitude is unclear: on the one hand, it seems like the group is becoming consolidated in the trade sector; however, we must consider that the regulations which this type of fund (PE) is subject to oblige investors to remain at least five years without undoing their investment. Perhaps the compulsory nature of these investments is giving rise to some sort of permanence culture in the sectors it invests in. This, however, cannot be stated categorically.

The investment group has sold certain parts of the DinoSol group, but it seems that these sales have been carried out to obtain atypical resources or to improve profitability when a good purchase offer has appeared. Neither these sales nor other acquisitions made by the group seem to indicate a new strategic direction.

They seem to be sales to 'cash in' when a good specific offer turns up, as in the case of selling the establishments in Ávila to the group Árbol, now dominated by savings banks in Castilla-León. In the case of the sale of assets in Catalonia, these sales are related to a competitive strategy perspective; the group did not enjoy a favourable image and position in Catalonia.

7.12 Conclusion: lessons to be learned from this case study

We have pointed out that the case relating to the acquisition of DinoSol group by the Permira investment group had two relevant elements. A first characteristic is related to the case itself as an example of the coexistence of economic mechanisms belonging to the globalised economy and strategies born in the local sphere. A second characteristic is related to the management model followed by the investment group, which has adopted the search of agreement and negotiation, as opposed to forceful solutions, to solve the conflicts arising in the acquisition process.

The lessons learned from the case are related to the position taken by Permira in view of the current financial crisis and slowing down of real economy. In this case, Permira, like other groups managing collective investments, is trying to face a situation that is very complex with regard to its interests. Collective investment schemes of the PE type have followed a highly leveraged buying model. This is a situation that will no longer be repeated as the lack of liquidity blocks access for debt from outside (above all on the banking side). Funds will have to use own funds and take on risk levels that will make it impossible to obtain financial margins such as those achieved until a short while ago.

Hence, the leveraged buying model cuts out risk for the acquirer, multiplies the incentive to buy and reduces the quality of analysis of the assets of the 'bought' company which has been seriously affected by the financial crisis. This is the cocktail that has justified the ferment of activity of the collective investment schemes in the last few years and which has just vanished. There is no money available to 'leverage' and all investments must be reviewed that are committed to transactions where the return is uncertain.

In these circumstances the fund management teams tend to guard their portfolios, i.e. to keep an eye on the quality and betterment of the company assets they have taken. On this point it seems that the most likely prospects tend towards a certain closing in the relationship of funds with companies invested in.

Yet on the other hand, the operating conditions in investee companies do not generate the returns that investors in the fund expect. This means that fund managers are not exactly diverting their focus of interest from searching out pre-crash returns. Whether they find them or not is something that nobody can say for sure at this time.

Therefore, this is an interesting example of a PE takeover in a sector, retailing and supermarkets, where PE has not been particularly big, but where in an increasingly competitive environment, firms can get into difficulties. Given increased competition and deregulation and in the context of the present world financial crisis, Permira faces real challenges with DinoSol, but the supermarket chain would have faced such challenges anyway.

The case shows nicely how a PE company works, setting financial parameters, but then devolving most aspects of management to local managers, many of whom are incumbent managers. This is particularly the case with industrial relations type issues.

There has been a definite impact on industrial restructuring. Some stores have been closed, but other new ones opened where there are deemed to be better opportunities. This has led to some job loss. However, most of this has been covered in a Plan, agreed with the unions. This would seem to be an example of how the threats and opportunities of a private equity take-over seem to have led to greater worker involvement in a wider range of issues.

In Spain the model of highly leveraged acquisition with an increasing ratio of risk dispersal towards the total amount of debt and protection of one's own reserves is a 'business model' that will hardly repeat itself in coming years. Whether from this dilemma it turns out that collective investment schemes are going to bolster their relationships with companies invested in and create expertise in connection with the sector, business or management of the companies invested in, or on the other hand spread their assets into other investment activity is something that cannot be confirmed or denied right now.

Developments in the case of Permira-DinoSol lead us to this situation whereby, this being an exceptional case, an investor in risk funds changes their normal habits (buy-streamline- restructure-sell) and introduces a sector business logic and includes a re-structure method that is innovative within the domestic context and more socially responsible.

8 Zelmer/Poland: A case study of a PE investment

8.1 Overview of PE, HF and SWF investments in Poland

Poland has the lowest absolute level of PE activity among the six countries studied. Neither fundraising nor investment activity accounted for more than € 1 billion in any of the years examined. PE investment activity shifted from a fairly balanced distribution at the beginning of the period (e.g. 11% of investment in the seed stage) to a very high concentration in buyout activity in 2006 and 2007 (accounting for 92 % and 82 % of investment activity in those two years, respectively).

Identified HF equity positions were also much smaller than in the other five countries (the largest position at the end of 2008 accounting for 0.4 % of shares outstanding). All of the top 20 identified SWF equity positions were accounted for by Norges Bank.

8.2 Zelmer – Private Equity as part of a privatisation and growth strategy

Introduction – Why the case was selected

Zelmer has been selected as a case study because it is a typical example of the involvement of a private equity fund in the privatization and transformation of a company. The investor had targeted Zelmer several years prior to the actual investment and had experience with restructuring and how to transform acquired assets into market-oriented companies, thereby creating value for the fund investors.

Economic Reform, restructuring and the impact of private equity in Poland

Since 1989, Poland began a process of economic transformation with the aim of establishing a market economy. Aggressive monetary reform, privatizations and institutional reform were undertaken to position the country as a qualified candidate for EU membership and then as a full member. Due to a dynamic internal market, a qualified workforce and attractive pricing of assets, Poland was able to attract substantial foreign direct investments both in terms of strategic acquisitions of industrial assets and also through financial investments in the rapidly developing stock market. Following the lead of the large corporations many mid size companies established subsidiaries allowing them to produce for both the internal market and for export. As a consequence the foreign trade pattern changed substantially, with 70% of this trade taking place within EU today. In addition to increasing investments from abroad, small local companies also quickly grew in size and market share. Local ownership continues to predominate in mining, metal, chemical, energy and utilities as well as among the mid size companies in service sector and some segments of manufacturing.

During the 1990s the majority of privatization took place through either direct sales to strategic investors (i.e. multinational corporations) or through a sale of shares on the stock exchange (IPO or initial public offering). Some industrial assets were distributed or sold to managers and employees, which in turn were bought up by private holdings established especially for that purpose. Hedge funds were involved in some schemes. In late 1990s the IPO process started to dominate as the main channel for privatization. This was facilitated by the creation of the pension funds, which needed to invest at least some of their funds in tradeable securities. Private equity in Poland has at least two origins. One is domestic, financed through capital realized by individuals in the early stages of privatization. These funds are frequently the investment vehicles for owning managers of privatized companies who later diversify their holdings, in part by creating private equity like organizations. The second category of capital providers includes financial investors from abroad, which were structured as private equity companies from the beginning. In the second category currently there are 4 types of private equity funds in Poland:

- funds established on the basis of the initial support from foreign public institutions (e.g. the Polish-American Enterprise Fund and Enterprise Investors, which manages multiple funds),
- funds established on the basis of an initial private capital investment in specialized funds (e.g. MCI or White Eagle Industries),
- subsidiaries of regional funds operating in all of Central and Eastern Europe (including Poland) (e.g. Innova/98),
- Business Angels – non-institutional individual investors (e.g. Polish Network of Business Angels).

The activity of the private equity is now established and most private equity investors belong to a professional association (Polskie Stowarzyszenie Inwestorów Kapiitałowych). Most private equity investments went into the production of consumer goods and services, including distribution. Also worth noting is the strong presence of private equity in the telecommunication sector and information technology.

8.3 Profile of the company and the investor⁴⁴

Zelmer S.A.

The company was established in 1951 as a state-owned company in the city of Rzeszów in southeast Poland. The company's main areas of business are production and wholesale distribution of small electric household appliances. Historically it was the biggest producer of such appliances in Poland. As will be seen in the case study, under the new ownership of private equity starting in 2004 it was able to further strengthen its position. Historically the company sold goods under its own brand mainly in Poland. It also had significant production activity for foreign companies in the sector which were selling these products under their own name. The company was strongly vertically integrated, performing many sub-processes internally. The company had already been targeted for

⁴⁴ This case study is based on information provided by the Zelmer company and Enterprises Investors as well as interviews with management representatives.

privatization at the beginning of the 1990s. Between 1992 and 1997, while Zelmer was still a state company, it created 16 private companies which were intended to take on substantial portions of the industrial activities. This process was stopped in 1998 and most of core functions have been re-integrated into one company. As a consequence it was possible to transform the company into a joint stock company (S.A.) whose shares were fully owned by the Treasury. Its financial position was however far from what was needed to sell it on the market for an adequate price. During 2001-2003 the new management board undertook substantial downsizing activities, enabling the company to break even. In 2003 the Zelmer management board made a proposal to the Treasury to sell its shares in the company through an IPO.

Enterprise Investors

The investment activities of Enterprise Investors started on the basis of the Polish-American Enterprise Fund (PAEF), which was created in May 1990 with \$ 240 million of capital. PAEF was a non-profit American corporation⁴⁵ established to promote private sector development in Poland and to initiate activities such as equity investments, loans, donations, and technological support. Successful work of PAEF led to the founding of the Polish Private Equity Fund I and II with \$ 151 million capital from PAEF and other private owners. In the following years Enterprise Investors created other investment funds. Today, Enterprise Investors manages a group of funds with a total capital value of \$ 1.1 billion. Enterprise Investor's funds invested more than \$ 750 million in 93 companies. It is one of the largest foreign investors and is the biggest private equity group in Poland as well as in the Central and Eastern European region. Up to 2009 the fund management already had sold off 61 of its investments, thereby multiplying the original capital invested by 2.5 times. The team of Enterprise Investors includes about 20 persons.

Enterprise Investors was or is active as an investor in companies in the following sectors: financial services (Magellan Ltd.), IT, telecommunications and media (Orange Romania SA), pharmaceuticals and health care services (Medycyna Rodzinna SA), consumer goods (W.Kruk SA) and manufacturing (Zelmer and other investments). Enterprise Investors is specialized in investments like: financing fast-growing companies (Lukas Bank SA), capitalization in conjunction with obtaining a listing on the stock exchange (Eldorado SA), start-ups (Polish Energy Partners SA), restructuring (Carnaud-Metalbox-Gopak) and management buy-out forms of privatization and joint ventures (Donnelly Polish-American Printing Company).

It is very important to emphasize that Zelmer was not the only investment of Enterprise Investors in the household appliance sector. Enterprise Investors were also present in companies like Polar, which is a well-known refrigerator manufacturer, or Stomil Sanok, a rubber and elastic components producer in Poland. Enterprise Investors therefore had previous experience in the sector prior to investing in Zelmer.

Enterprise Investors was successfully operating in Poland but also decided to invest its capital in other countries in Central Europe. Polish Enterprise Fund IV was set up for this purpose. The capital for this Fund was committed by financial institutions, pension funds and insurance companies from Western Europe and the United States. The value of equity was \$ 217 million. Poland's accession to European Union in 2004 led to greater interest in Polish market. It created another opportunity for Enterprise Investors to expand its activities with the capital of € 300 million for Polish Enterprise Fund V. It was provided by investors with experience from the previous funds as well as from western

⁴⁵ PAEF is one of ten enterprise funds created under the Support for East European Democracy (SEED) Act and the Freedom Support Act. It has become a major U.S. government foreign economic assistance success story. In 1990, USAID gave a \$ 240 million grant to PAEF, which then turned it over to private citizens in Poland, many of them venture capital investors. Their mission was to invest the money in fledgling businesses in Poland to help the country's transition to a free market economy.

financial companies new to the region. The most recent fund (Polish Enterprise Fund VI) was created in 2006 with a total value of shares of EUR 658m subscribed by private companies from Western Europe and the United States. The Fund was established in only 3 months and was two times oversubscribed. Also it was the first time Enterprise Investors decided to invest in countries outside of the European Union – namely in Croatia and Ukraine. In 2008 Enterprise Investors decided to open its first venture capital fund under the name Enterprise Venture Fund I with total capital of € 100 million. The investments of this fund range from € 1 million to € 5 million per project. It finances mainly small and medium enterprises in the expansion phase in technology and traditional sectors in Poland and in other Central and Eastern European countries.

Enterprise Investors development and capital volume

	Fund	Year of establishment	Value of capital
1.	Polish-American Enterprise Fund	1990	\$ 240 million
2.	Polish Private Equity Fund I	1992	\$ 151 million
3.	Polish Private Equity Fund II		
4.	Polish Private Equity Fund III	1997	\$ 164 million
5.	Polish Private Equity Fund IV	2000	\$ 217 million
6.	Polish Private Equity Fund V	2004	€ 300 million
7.	Polish Private Equity Fund VI	2006	€ 658 million
8.	Enterprise Venture Fund I	2008	€ 100 million

Source: Enterprise Investors

Enterprise Investors funds invested in companies in a broad range of economic sectors such as manufacturing/services, consumer goods, pharmaceutical industry/health care, IT/telecommunications/media, financial services. The fund is specialising in the following kinds of investments:

Enterprise Investor is specializing in following kinds of investments:

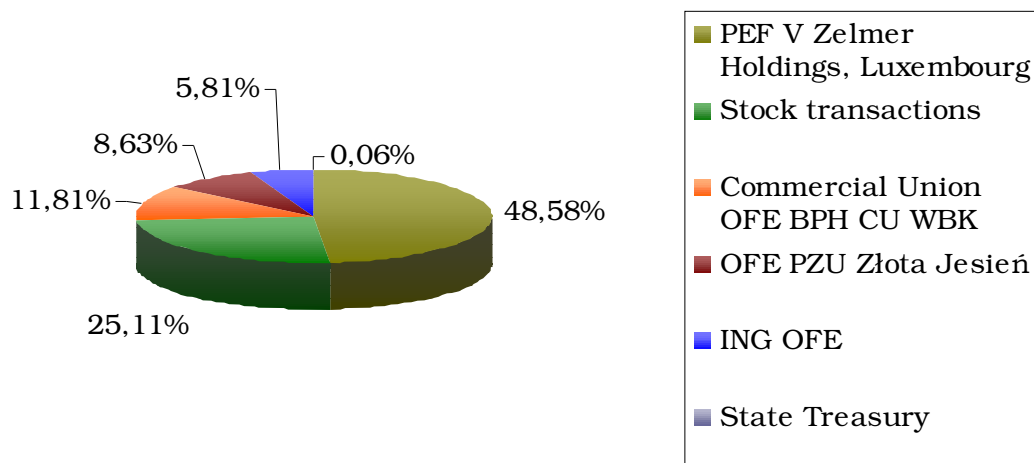
- ☐ buyout of fast developing enterprises,
- ☐ equity increase in conjunction with an initial stock exchange listing,
- ☐ start-up finance,
- ☐ restructuring/turnaround,
- ☐ management buy-out and buy-in,
- ☐ joint venture.

8.4 The investment

Once the proposal to privatize through an IPO was accepted, Enterprise Investors offered to acquire substantial portion of the shares sold. The rest of the shares offered were successfully sold to other institutional investors as well as individual investors. 15% of shares were distributed to the employees. The Treasury held a very small part as well as a seat on the Supervisory Board. The Treasury holding was sold in June 2009.

On 30 November 2004 The Securities and Exchange Commission admitted the shares of Zelmer to public trading. On 27 January 2005 the shares of Zelmer S.A. were listed on the Warsaw Stock Exchange. The majority stake was acquired by Enterprise Investors through the investment vehicle PEF V Zelmer Holdings.

Current shareholders of Zelmer (2008)



Source: Zelmer

Strategy of the financial investor

The strategy undertaken by the financial investor was to transform the company into a market oriented competitor by building on its brand as well as exploiting the possibility of expand the product portfolio based on imports from China. From the beginning the intention was also to reorient the focus of the company to East Central European markets, selling there under Zelmer name to build brand value. This in combination with programs to increase manufacturing productivity was to increase the company's value over time.

The supervisory board under the leadership of Enterprise Investors set the objectives for the company and also introduced an incentive program in the form of stock options. The main areas of investments were marketing and international sales. Investments have also been made in research and development and to some extent in production. The strategy was to increase the company's flexibility and to maintain an adequate balance between locally manufactured products and imports. The investor rightly anticipated the positive impact of Poland joining the EU as well as demographic developments. The construction boom, inflow of money from abroad, local and foreign investments all resulted in an increase in the purchasing power of the population. A dynamic pricing policy, strong brand recognition, flexible logistics and an active sales policy were identified as elements of the strategy to be implemented.

Consequences for core business

When Enterprise Investors decided to invest in Zelmer in 2004, the company was confronted with several economic problems. Under the management of the former main owner (the State Treasury) many decisions had been influenced by political considerations. This prevented the implementation of a stable long term strategy for the company. To have a well-known brand and a historically strong position in the Polish market was not enough to compete successfully with new rival companies and brands from abroad. Enterprise Investors brought strategic insight and operational management capacities to Zelmer. After an extensive financial and operational audit through an external consulting company, Zelmer started a large-scale reorganization. The Enterprise Investors' involvement was particularly intense in this first period (from 2004 to 2005). After this time the investor delegated operational decisions more and more to the company's managers, who had partly been replaced by new managers.

During this process of restructuring Zelmer reduced the number of employees by approximately 300 to about 2,200 workers. In the years 2006 and 2009 the company implemented several Voluntary Departure programs. At the same time employment conditions have been adapted to bring more flexibility and to allow the company to cope with demand fluctuations. While continuing to develop the range of its own products the company aggressively expanded the portfolio by adding imported products.

Economic development of the company 2004-2009

Based on Company consolidated reports	2001	2002	2003	2004	2005	2006	2007	2008
Revenues from sales (K PLN)	316 725	270 700	275 844	310 799	299 343	340 391	420 464	465 443
Operating results (K PLN)	-14 289	13 745	16 703	27 484	30 194	37 641	47 113	32 299
Gross profit (K PLN)	-19 793	13 231	19 963	28 904	30 019	37 617	46 983	30 891
Net profit (K PLN)	-18 786	7 902	13 000	21 941	23 414	30 520	34 520	24 720
Depreciation (K PLN)	30 024	27 970	25 909	8 579	8 701	8 970	9 520	11 821
EBITDA (K PLN)	15 735	41 715	42 612	36 063	38 895	46 611	56 633	44 120
Assets (K PLN)	258 050	225 483	256 436	297 075	317 540	346 042	371 679	444 407
Own capital (K PLN)	165 411	173 313	187 747	232 329	255 219	254 141	269 498	262 290
Number of shares (K)	15 200.000							
Earnings per share (PLN)	-1.236	0.52	0.855	1.443	1.54	2.008	2.271	1.626
Book value per share (PLN)	10.882	11.402	12.352	15.285	16.791	16.72	17.73	17.256

Source: Zelmer

The return to profitability actually occurred prior to the sale of a majority stake to private equity. Since 2004 net profit was growing regularly, reaching more than 34 millions zlotys in 2007. The 2008 result was negatively impacted by adverse movements in currencies and the valuation of currency options. After focusing on operational fundamentals in 2004 and 2005, in 2006 Zelmer started rapidly expanding its product portfolio and exports, producing impressive growth in EBIDTA from 38 million zlotys in 2005 to 56 million zlotys in 2007.

Particular attention was paid during this period to the profitability of each product category and the careful selection of sales channels. As a consequence, the organization of exports was modified to ensure direct presence in target countries,

In terms of production Zelmer continues to produce its flagship products (vacuum cleaners, slicers, juice extractors) in Poland in Rzeszow plant. On the purchasing side, programs implemented early on improved profitability and thereby the competitiveness of production. Also wages and salaries were managed very carefully.

Zelmer case: chronological overview

2001 - July: The Minister of the State Treasury made a statement regarding the commercialization of the state enterprise Zelmer, which was to be transformed into a public limited company with the State Treasury as the only shareholder. **August:** The commercialization of the company took place. Members of new Board decided to start restructuring activities.

2004 - November: The Securities and Exchange Commission authorized the admission of Zelmer's shares to public trading.

2005 - January: Zelmer shares were quoted on the Warsaw Stock Exchange for the first time. Zelmer S.A. obtained a certificate as a stock exchange-listed company. Polish Enterprise Fund V administered by Enterprise Investors purchased a 24.9% share in Zelmer from the State Treasury.

April: Enterprise Investors became the biggest shareholder in Zelmer through PEF V Zelmer Holdings Fund.

2006 - December: Zelmer initiated a voluntary departure program at its sites in Rzeszów. 130 employees decided to leave the Company.

2007 - May: Zelmer is willing to buy Serbian company from the same branch until the end of 2007 after its privatization. The Serbian company has a well known brand name in the Balkans and produces the same type of household appliances. Other plans related to abroad were focused on Central and Eastern Europe, especially on increasing the export and sales network.

August: Zelmer signed a contract with Avans International company to sell household appliances through the Avans sales channel in Poland. The value of the contract was PLN 28m. It was the biggest contract letting Zelmer increase its presence in the Polish market.

2008 - January: Zelmer announced new strategy plan – “Development Plan – Zelmer Pro 2010”. According to this document the company wants to increase its shares in European markets, especially in Central and Eastern Europe. Another strategic point in the plan was to expand the number and type of appliances produced for the first time by Zelmer. In this connection the company established a Planning and Logistical Centre and New Products Implementation Centre.

February: Zelmer decides to cooperate with the Russian company Nikita. This Moscow-based company agrees to sell, distribute and promote Zelmer’s products in all of Russia (the biggest market abroad Poland in Zelmer’s portfolio). The value of the contract is EUR 33m.

December: As was the case for many other companies in Poland Zelmer had problems with currency options because of world financial crisis. As a result the company was forced to change its financial plans for at least the next two years.

2009 - January: Once again the company decided to initiate a voluntary departure program. Employees can receive 8 months salary and participate in an outplacement program.

8.5 Development of employment

One year after the PE investment several (mainly qualitative) changes in employment were implemented. Those changes were strongly linked to the new strategy of increasing flexibility and productivity and of shifting resources from production to sales and support, which were necessary to compete in the marketplace. It is important to note that Zelmer was restructured between 2001 and 2004 under state ownership to improve its financial situation and prepare it for privatization. Therefore substantial downsizing was not needed under PE ownership. The first change introduced by PE in the company was to hire a temporary work force. This practice became permanent since 2006 with the initiation of a new model of employment. Temporary workers are hired during peak production times. Usually the largest growth of seasonal employees takes place in the second half of the calendar year.

Zelmer Employment Levels, 2003-2008 (year-end)

Employment	2003	2004	2005	2006	2007	2008
Regular		2,327	2,312	2,277	2,250	2,034
Temporary	-	-	-	410	450	488
Total		2,327	2,312	2,687	2,700	2,522

Source: Zelmer

The second important structural change was the increase of sales and support staff (figures before 2006 are not available).

Zelmer Employment by Division, 2006-2008

Section	2006	2007	2008
Production	2,424	2,398	2,143
Sales	65	91	97
Support	198	211	282
Total	2,687	2,700	2,522

Source: Zelmer

The tables above demonstrate net effects in employment. The company reduced the core workforce and sold off some non core activities, but at the same time increased overall employment levels by hiring temporary workers.

The workforce reductions made in Zelmer to date usually involved selected employees acquiring early retirement benefits. Dismissals were made across the whole company, not only in some sections. All of these changes were made in agreement with trade unions. In 2006 a Voluntary Departures Program was introduced, in which 147 employees participated. A similar program was repeated in 2009. Another big change in employment also took place in 2006, when 133 employees were moved out of the core company as result of the spin-off of "META-ZEL" Ltd. Company. This company took over Zelmer's casting operations, in part through a property rental agreement with Zelmer.

Workforce reductions at Zelmer, 2003-2008

2003	2004	2005	2006	2007	2008
	114	48	355		178

Source: Zelmer

The pay system was also modified. The objective was to keep wages somewhat higher than the local average (Podkarpackie Province) to attract and retain qualified labor but to also keep costs under control.

Average gross salary at Zelmer, 2003-2007 (PLN)

Area	2003	2004	2005	2006	2007
Zelmer		2341,97	2487,92	2678,84	
Podkarpackie Province	1876,93	1940,50	2001,53	2088,85	2259,00
Poland	1950,01	2018,59	2081,76	2179,57	2372,82

Source: Zelmer

Enterprise Investors triggered several changes in HR policy area at Zelmer. Specific programs started in 2007 are still in place. During this time the company started to implement new policies focusing on adequate support in key areas of the company's activity. All the activities were aimed at the effectiveness and optimization of employment. These policies resulted in an increase in competences and qualifications in all departments ranging from production to research activities.

The company also decided to organize workshops to improve employees' qualifications. The workshops were successful in bringing in new expertise needed to continue existing activities and improving knowledge about the company and its financial and management activities. An additional benefit of the workshops was to improve communication between different groups within the work force (workers, management, trade unions etc.). Workshops, courses and programs were mostly connected with financial and management skills and included the following:

- ☐ Strategy cascading – workshops for key managers
- ☐ Manager's Academy – courses for foremen and department heads in production
- ☐ Project management – for selected managers
- ☐ Finance for non-specialists – managers in key positions
- ☐ Talent Development Center
- ☐ Assessment Development Center – for 16 employees with the highest development potential
- ☐ Language courses

It is important to highlight that these new policies were initiated since Enterprise Investors invested in Zelmer. The activities successfully supported the strategy to build a new level of commitment and involvement in Zelmer.

Private equity investment in Zelmer was received by employees and trade unions with concerns. This was a typical response to the entry of a new owner who was perceived as financially aggressive. Enterprise Investors decided to react to this very quickly and decisively in an assertive manner. A direct dialogue with workers was initiated and information about the principles and objectives was communicated with a high degree of

transparency. Enterprise Investors representatives met with trade unions to inform them about intentions towards Zelmer, including strategy and organization changes, expectations related to these changes, decisions made, and so forth. At the same time the investor decided to give Zelmer's management more local autonomy.

8.5 Consequences for production organization

The strategic changes which occurred after the entry of the private equity investor were connected with management structure, production profile, sales channels and employment. To change its market position the company started to expand the product portfolio. The previous range of products was not large enough to compete with other well-known brands in Poland and in the region. Competition for access to stores was particularly intense. Zelmer had to introduce some new types of appliances already offered by the competition. Zelmer increased the number of products in the same way as such brands like Moulinex or Electrolux, namely through sourcing from China. The Zelmer brand was a solid selling platform and customers accepted new products with confidence. After 2006 the range of products increased from 8 categories to a total of 26 categories in 2008 and is still growing.

Zelmer Product Portfolio Pre- and Post-2006

Categories of electric products up to 2006	New appliances introduced after 2006	
vacuum cleaners food processors juice exactors mixers mincers cutters slicers kettles	microwave ovens irons scales coffee makers water filters grills toasters fryers steamers	hoods air-conditioners humidifiers ventilators hair-cutters hair-driers rectifiers pots (nonelectric) frying-pans (nonelectric)

Source: Zelmer

Zelmer continues to augment its sourcing capabilities and expand its portfolio. In 2008 the company introduced a three-year development strategy "Zelmer PRO 2010", which is mainly based on new product categories and new types of vacuum cleaners. The strategy assumes sales growth of PLN 700 million (about 20% per year). It means that growth would be twice as fast as the market as a whole. It would also increase Zelmer's share in the Polish household appliances market to about 30%. The current financial crisis however has slowed the growth rate of the market, resulting in a challenge to achieve its growth plans. Up to 2008 however the new strategy had been successful.

Zelmer's Sales in Poland, 2005-2008 (PLN)

	2005	2006	2007	2008
Hitherto products	186,230,000	207,903,000	218,520,000	229,000,000
New products	-	11,173,000	60,100,000	107,000,000
Total	186,230,000	219,076,000	278,620,000	336,000,000

Source: Zelmer

The second important element of the new strategy was the development of Zelmer's direct distribution activities abroad, primarily in East Central Europe. After the private equity investment this type of business activity became very important. Before the acquisition Zelmer was selling its products mainly in two areas:

- ☐ Western Europe (Germany, Switzerland, France) and Turkey (on a private label basis);
- ☐ Central and Eastern Europe (Russia, Ukraine, Baltic countries, Czech Republic, Slovakia, Hungary, Romania) (via indirect distribution)

Active export growth was especially promoted by improving distribution channels by establishing subsidiaries in Slovakia (Zelmer Slovakia S.ro.), Czech Republic (Zelmer Bohemia S.r.o.), Romania (Zelmer Romania), Ukraine (Zelmer Ukraine T.B.O.) and Russia (Zelmer Russia o.o.o.). The company is still looking for new opportunities to expand sales abroad. For example in 2008 Zelmer started expansion in other Eastern European countries, namely Armenia, Belarus and Croatia.

Value of Zelmer's exports, 2005-2008 (PLN)

	2005	2006	2007	2008
Value of export	93,100,000	103,700,000	130,200,000	121,400,000

Source: Zelmer

It is also important to mention the outsourcing strategy of Zelmer. It was necessary to compete with importers offering cheaper products. The company undertook an attempt to set up production of appliances parts with other companies in Ukraine and Serbia. Unfortunately they were not able to meet Zelmer's standards. Today the only company which cooperates with Zelmer in the field of parts production is Bianor, a company in Białystok (northeast Poland), which makes plastic forms. Zelmer also decided to import some parts from China needed for vacuum cleaners – pipes, filters and bags. Zelmer is also bringing in more complete products from Far East (microwave ovens), which it then sells them in Poland and Central Europe. The current situation in the market place and the devaluation of the zloty improves the competitiveness of production in Poland. Zelmer continues to exploit this advantage by planning more investments in the manufacturing area.

The increase of revenues was possible thanks to a new marketing strategy actively implemented in Poland and as well as abroad. Active marketing was implemented in a manner never before practiced at Zelmer. After the PE acquisition Zelmer established a new department for the active promotion of products and the Zelmer brand. The promotion programs were re-oriented towards more effective media. Similarly the research and design departments were re-organized for more effectiveness. They had to react to clients' demands and to fulfill the strategy of gaining the position of prime supplier of kitchen appliances and re-enforcing leadership in vacuum cleaners. Today it can be said that those two targets have been achieved.

8.6 Comparison of company development with market and company Amica

A very good comparison of Zelmer to other companies operating on the Polish market would be to look at Amica. The market valuation Amica, one of the most popular white goods producers in Poland, continually declined during the last years. Meanwhile, with the exception of the past few months, the value of Zelmer grew. This disparity is striking, since both companies operate in the same strongly-growing market in Poland.

Polish GDP, 2004-2008

	2004	2005	2006	2007	2008
GDP (PLN mld)	885,342	964,569	1,033,720	1,167,456	1,271,700
GDP growth	5.3%	3.6%	6.2%	6.7%	4.9%

Source: Polish Statistics Office documents

Amica and Zelmer are active in similar markets and are both Polish brands. The first company was the market leader for large household appliances, and other gained leadership in small household appliances during the same period. However, here ends the similarity between them. With the time the development of both companies differs. Amica's long-term problems with profitability continued to deteriorate. Zelmer, by contrast, was able to improve performance and systematically built value.

Disparity in the value of both companies is surprising, especially since the markets of small and large white goods grew at a similar pace. Demand for household appliances

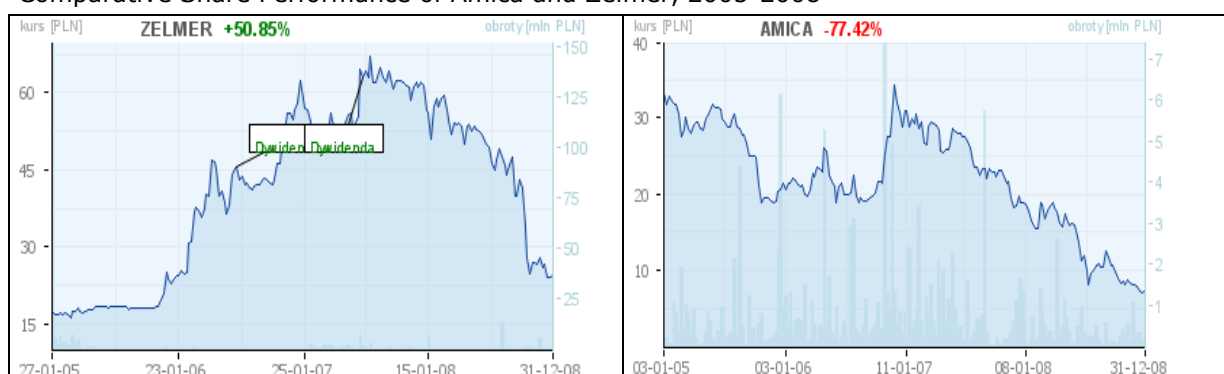
increased with the housing boom, as optimistic consumers moved into new apartments and houses and needed new appliances. In a short period of time (after the second quarter of 2007) the sales of large household goods jumped by 25%, amounting to € 800 million. The significant increase was a result of increased construction activity. The market for small household appliances grew almost as rapidly in the same period (by 21.7%) to € 537 million.⁴⁶

Zelmer took advantage of the prosperity and managed to increase revenue by 27%, with the most dynamic product sales in the categories of vacuum cleaners (+45%) and juice extractors (+38%). Export sales increased by 34%. The company from Rzeszów managed to increase sales profits and EBITDA margins.⁴⁷

Revenues of Amica were also growing. Sales in the domestic market increased by 25%. Export sales increased by 36%. Despite the overall increase in revenues by 22% the company was not able to improve the bottom line. Amica's manufacturing and sourcing strategy was not dynamic enough. The company results were impacted by an increase in raw material prices starting in 2006 and a decline in the euro exchange rate.

Looking at the share prices of Amica and Zelmer, we see the attention paid by investors particularly to bottom line performance. Since Amica's finances were deficient, its market valuation was also deficient. From the beginning of the year its market value fell from € 250 million to less than € 200 million. Zelmer was worth about as much at the beginning of 2005 when it went on to the Warsaw stock exchange. In 2007 its valuation was around € 340 million. The trend for Amica was the opposite. Sales of the company were stable for several years at more than € 1 billion. The rate of market price-to-sales for Amica was 0.15 and was one of the lowest in the market. The same indicator for Zelmer oscillates around 2.5 and was significantly above the market average (1.7).

Comparative Share Performance of Amica and Zelmer, 2005-2008



Source: www.money.pl

While Amica was losing the market share Zelmer became the leader in vacuum cleaners and also an important player in new categories, especially microwave ovens and irons. Zelmer's market share of these products is still increasing.

Polish Market share of Zelmer's new products; 2006-2008

New products	2006	2007	2008
Microwave ovens	6%	15%	18.5%
Irons	5%	10%	16%

Source: Zelmer

⁴⁶ M. Zbiejczek Zelmer obala mit wielkiej Amiki, „Puls Biznesu” 13.09.2007.

⁴⁷ Sprawozdanie z działalności emitenta w 2006 r.

Comparing the company to other market leaders from regions producing small household appliances in the Polish market, we notice that Zelmer is the most recognized brand.⁴⁸ The Zelmer brand, which Poles are familiar with for more than half a century, is one of the most frequently purchased in Poland.

It is also worth noting the fact that this brand was successfully sustained after the private equity acquisition. Zelmer has successfully coped with the entry of many western brands to the Polish market such as Braun, Electrolux and Bosch.

Based on the facts reviewed and the strategy executed by the management board appointed by the new owners led by Enterprise Investors, we can see a substantial transformation of the company in practically all aspects. From a passive, internally focused company losing market share Zelmer became a leader in small appliances in Poland and a modern market oriented company with sound financials.

8.7 Other known investment of the financial investor in the same sector

Enterprise Investors is present in many companies in and outside of Poland. It can be noted that it is not limited to one particular industry. It is present in companies operating in such diverse areas as banking, cosmetics production or tour operators. Many of these companies are quoted on the Warsaw Stock Exchange.

Among these companies few are related to the production of household appliances or parts for such devices. Among the companies that are similar to Zelmer are Gametes (furniture accessories producer) and Wema (bathroom equipment seller). Rather than specializing in a specific sector, the fund specializes in some typical strategies, implementing these activities in different companies after acquisition until the time of exit.

Similar patterns of applied strategies in cases can be found in cases such as Eldorado, Stomil Sanok, Lukas Bank and Polfa Kutno.⁴⁹ Two of them – Stomil and Polfa – are companies previously belonging to the State Treasury. Strategies introduced in these companies are in line with those that can be observed at Zelmer. Among these are:

- ☐ Introduction of strategic and industry consultants (Polfa Kutno, Eldorado);
- ☐ Restructuring of employment (Stomil Sanok, Polfa Kutno);
- ☐ Recruitment of top executives for key positions in management (Polfa Kutno, Lukas Bank)
- ☐ The introduction of stock options for management (Stomil Sanok)
- ☐ A focus on strong product development capabilities (Stomil Sanok, Polfa Kutno)
- ☐ Increasing exports (Stomil Sanok)

Similar strategies were also implemented in other companies in which Enterprise Investors was present. One company is particularly worth mentioning. Polar from Wrocław (southwest Poland) is a company which also manufactures household appliances, mainly refrigerators. The company was also privatized. Since investment in the company (from 1997 to 1999) Enterprise Investors had to deal with restructuring, which was performed by the consulting company. Consultants have prepared the company to change, including downsizing and changes in organization and management, as well as introducing product re-engineering. The activity of the fund resulted in profits. In Polar, there were active two trade unions, and the restructuring program encountered challenges. At the same time, it became clear that the Polar brand did not have as much value as expected. Consequently Enterprise Investors decided to sell the shares, which were finally bought up by Whirlpool.

⁴⁸ P.Otto Marki handlowe z PRL są warte nawet 5 mld zł, „Gazeta Prawna”, no 183, 18.09.2009.

⁴⁹ Central and Eastern Europe Success Stories. EVCA Special Paper, EVCA Publ., Zaawentem 2004.

The previous experience with Polar helped to prepare Enterprise Investors to invest in Zelmer in an appropriate manner. At the same time, strategies previously applied to many other companies have been adjusted and successfully implemented to Zelmer.

Enterprise Investors' Company Portfolio

Company	Profile	Country
AVG Technologies NV	IT	Czech Republic
Bio-Profil Sp. z o.o.	Cosmetics production	Poland
DGS SA	Packaging	Poland
Dystrybucja Polska Sp. z o.o.	Bulk mail delivery	Poland
Gamet SA	Furniture accessories production	Poland
Harper Hygienics SA	Hygienic and cosmetic products	Poland
Jaan Group	Screen production	Poland
Kofola-Hoop SA	Beverage production	Poland
Komfort SA	Floor covering shops	Poland
Kruk SA	Public liabilities management	Poland
Macon Deva SA	Construction materials production	Romania
Magellan SA	Financial services for the health sector	Poland
Nay a.s.	White and brown goods selling	Slovakia
Novaturas UAB	Tour operator	Lithuania
PharmaSwiss SA	Pharmaceutical sales and services	Czech Republic
Siveco SA	IT	Romania
Skarbiec Asset Management Holding SA	Financial services	Poland
STD Donivo	Transportation services	Slovakia
Wema SA	Bathroom equipment sales	Poland
Zelmer SA	Small home appliances production	Poland

Source: Enterprise Investors

8.8 Exit strategy

As of today Enterprise Investors is still investing in Zelmer. Describing an exit strategy can thus only be done in hypothetical terms. From the beginning private equity paid particular attention to sound financial results, predictability and reliability of strategy as well as a strong management team demonstrating capability to autonomously and assertively operate in the market place. The financial crisis, which started in 2008, has changed the outlook for exit. Even though Poland continues to enjoy growth in industrial production and consumption in the first few months of 2009 the slow down is expected to hit in the second half of 2009. It is difficult to predict how much it will impact the small appliances markets. It is probable that the impact will be less than for the whole white goods market, but still for the overall market a slowdown in growth is to be expected. The overall mergers and acquisitions market has also slowed down due to lack of resources and risk aversion. It will be important to see to what extent the flexibility built into Zelmer's strategy is sufficient to protect its bottom line, which in turn would increase the attractiveness of Zelmer for pension funds as solid long-term investment. One can also speculate on the attractiveness of Zelmer for strategic investors in the same sector who want to consolidate their position in this part of European market and to acquire a competitive manufacturing and logistics asset.

8.9 Lessons to be learned

The Zelmer case shows influence of private equity funds on a company which was formerly owned by the State. The old Zelmer management had not been able to develop and pursue a stable growth strategy. The PE investors helped to introduce changes and to adapt to market demands. The direct restructuring in terms of the number of employees and production sites was limited. The key instrument used by PE was to improve operational performance and to build on the strong value of an intangible asset, i.e. the well known brand name Zelmer. A marketing strategy in Poland combined with expansion to other regional markets in Eastern Europe led to an improvement in profit-

ability which allowed further investments, mainly in an active marketing and distribution strategy. As far the human resources aspects are concerned the new owners were able to create a solid group of middle level managers devoted to the company's objectives. This will be a key factor for further sustainable growth. The private equity owner demonstrated an ability to learn from previous investments, adapt its strategy to a particular company, introduce effective programs and outperform similar companies by gaining market share and maintaining EBITA growth.

9 KUKA/Germany – A case of hedge funds investment

9.1 Overview of PE, HF and SWF investments in Germany

Germany is the third most important country among the six countries in this study with regard to private equity activity. Starting from a relatively low level of activity in 2003 (0.12% of GDP), investment by domestic PE funds had almost tripled by 2007. Investments by non-German PE funds still account for a substantial minority of investments in German companies. There has been a notable shift from seed and startup to buyout activity over the period, with buyout funds accounting for 84% of investment in German companies in 2007. In terms of GDP, however, PE investment in Germany is less than half the level of activity in the UK.

Although there had been a quite lively political debate on HF activities in Germany during the last years identified HF equity positions in companies listed in Germany were modest. In particular many smaller hedge funds are active, taking positions that are small in terms of the total shares of the target company but account for a significant proportion of the HF portfolio (6-9%).

Two of the top 20 SWF investments in companies listed in Germany were from the Kuwait Investment Office (a 7% stake in Daimler and an 8% stake in the Gea group). The rest are accounted for by Norges Bank.

9.2 KUKA – Active investors force industrial restructuring

Introduction: Why was this case selected?

In the national debate on the activities of private equity and hedge funds in Germany KUKA for some time was often quoted in the press as an example of the influence of financial investors on industrial development. After an initial investment in 2003 by Wyser-Pratte the discussions on the future development of the company not only dominated the annual shareholder meetings but also found their way into the headlines in the business press.

Beside the fact that the case has drawn some public interest KUKA is also for some other reasons a good example for a case study on restructuring and financial investors. In fact, the company was substantially restructured between 2003 and 2008. In this process KUKA concentrated on its core activities and sold almost all other assets. The behaviour of the institutional investors was very active in many phases. The case can be taken as an example of shareholder activism in Germany and Europe. And because KUKA is a listed company the impact of this restructuring process on the share price can be seen very easy. During the years between 2003 and 2008 a large number of institutional investors bought KUKA shares, among them several hedge funds. The case is also an example of hedge funds activities.

9.3 Profile of the company and the investor

Profile of KUKA⁵⁰

The name KUKA is derived from the initials of the company name "Keller und Knappich Augsburg" which was founded in Augsburg in 1898 by Johann Josef Keller and Jakob Knappich. It was first an acetylene factory for the production of cost-effective domestic and municipal lighting. KUKA later turned to electrical resistance welding and constructed the first electric spot-welding gun in Germany. Since this beginning in the early 20th century KUKA developed continuously. In 1956, KUKA built the first automatic welding systems for refrigerators and washing machines and delivered the first multi-spot welding line to Volkswagen AG. For Daimler-Benz, KUKA built Europe's first welding transfer line with robots in 1971. And in 1973, KUKA wrote history as a robotics pioneer by developing FAMULUS - the world's first industrial robot with six electromechanically driven axes. At the time the company was part of the Quandt Group in Germany.

In the 70s the Quandt group decide to merge KUKA GmbH with the Industrie-Werke Karlsruhe Ag into the Industrie-Werke Karlsruhe Augsburg Aktiengesellschaft, or IWKA AG. The new IWKA AG was also involved in the areas of packaging machinery, textile engineering, control technology, forming and machine tools. In 1979, the different activities of IWKA AG were transformed into legally independent companies and the stock corporation became a holding company for international mechanical and systems engineering. Following the withdrawal of the Quandt family, a public corporation is formed in 1980, with all shares floated freely.

In 1999 / 2000 IWKA bought the packaging machinery activities of the Rheinmetall group and the Anglo-American BWI group which made IWKA AG a leading provider of packaging machinery and plants. In exchange, the defence engineering companies were sold to Rheinmetall.

From 2004 onwards, IWKA AG concentrated on automation technology in the core business areas of robotics technology and plant and systems. Activities in the remaining business areas of process technology (fittings, measurement and control technology, and flexible elements), production technology (machining centers and turning machines) and packaging technology for the consumer goods industry were sold off gradually until early 2007. The company was then renamed KUKA Aktiengesellschaft and the headquarters were transferred to Augsburg. KUKA today concentrates on advanced solutions for the automation of industrial production processes.

Company structure

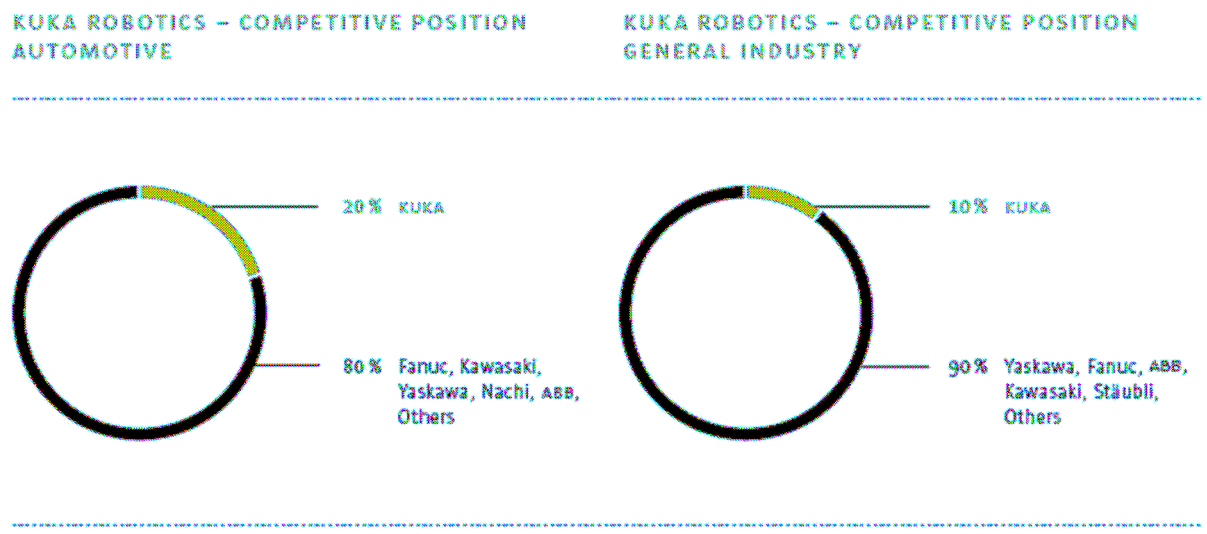
KUKA AG is a joint stock company listed on the German mid-cap share index, the MDAX. Today the KUKA Group consists of two divisions: robotics and systems. KUKA Robotics is one of the world's leading suppliers of industrial robotics. Its key fields of expertise are in the development, manufacture and marketing of industrial robots, controls, software and linear devices. The automotive industry is the main customer for the robotic section. The share of automotive orders of the robotics section's total volume rose from 42.7% in 2006 to 45.4% in 2007. Due to the financial crisis, orders received in 2008 declined in the fourth quarter. In all orders dropped by 14.1%, from € 197.3 million in 2007 to € 169.5 million in 2008.

Besides the automotive industry, KUKA robotics focuses on general industries, especially plastics and food, metals machining and processing, healthcare technology and logistics. Orders received in this section increased from € 141.8 million in 2006 to € 194.3 million in 2008, an increase of 37%.

⁵⁰ The case study is based on interviews with representatives of the KUKA management, Wyser-Pratte Management and a trade union representative of IG Metall.

In total the orders received by the robotic section increased from € 429.6 million in 2003 to € 464.4 million in 2008, an increase of 8.1%. The workforce of the robotics section increased from 1.834 in 2003 to 2.261 in 2008.

KUKA's market position

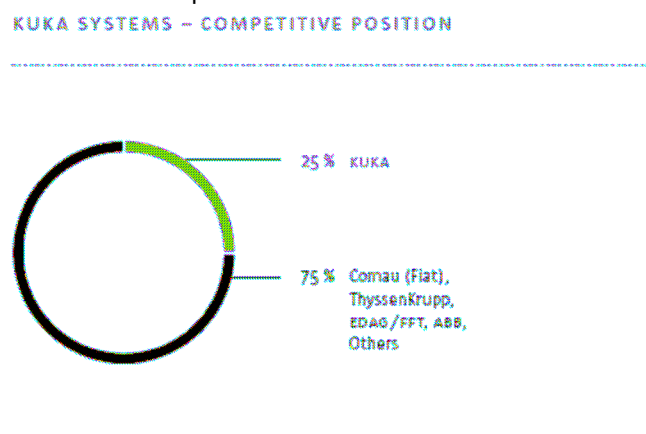


Source: KUKA Annual Report 2008

In the second part of the company, KUKA Systems offers automotive, aircraft and solar industry customers' automated solutions for their manufacturing plants. Acting as a general contractor, KUKA Systems plans and builds complete manufacturing systems for their customers. Its main locations are Augsburg (Germany) for the European market, Detroit (USA) for North American business and Shanghai (China) for the Chinese and Asian market.

The systems section is the larger business part of KUKA based on order volume as well as the number of workforce. Total orders received by KUKA Systems increased from € 651.7 million in 2003 to € 854.9 million in 2008, an increase of 31.1%. The workforce of the systems section increased from 3,194 employees in 2003 to 3,781 in 2008.

KUKA's market position



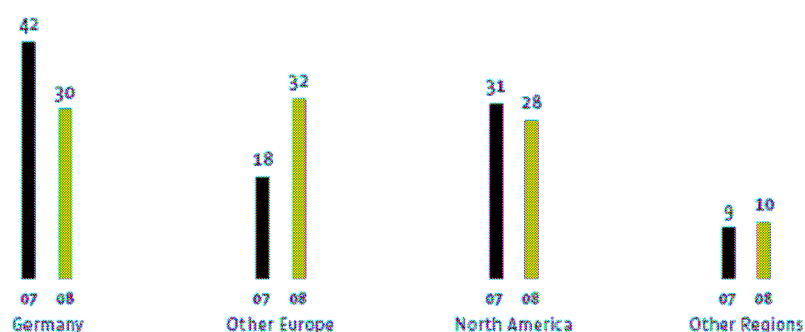
Source: KUKA Annual Report 2008

The KUKA Group is characterised by a high export share. The share of exports was relative stable at around 64% in the years 2004 to 2007. The current financial crisis has resulted in a decrease of foreign orders and the export share of KUKA has fallen to 59%.

KUKA – orders by region

KUKA GROUP ORDERS RECEIVED BY REGION

(share in %)



Source: Annual Report 2008

The automotive industry is the main customer with the highest range of application for robotics technology. In 2007 71.3% of the total orders KUKA received (robotic and systems) were attributed to the automotive sector. KUKA's long-term business goal is to win more independence from the automotive industry and gain a higher share in growth markets such as the aircraft and solar industries and in general industry sectors like medical and food industries.

KUKA – main economic indicators

KUKA Group		2003	2004	2005	2006	2007	2008
Orders received	€ mio	1062.4	1149.4	1090.2	1186.4	1343.8	1279.9
Sales revenues	€ mio	1122.5	1111.1	1051.1	1164.6	1286.4	1266.1
EBIT	€ mio	58.8	77.7	-53.4	16.7	70.4	52
in% of sales	%	5.2	7	-5.1	1.4	5.5	4.1
in% of capital employed	%	19.2	25.2	-21.9	8.1	41.6	21.5
Capital employed	€ mio.	206.6	308.2	243.7	205.2	169.4	242.2
Employees		5,144	5,443	5,463	5,580	5,732	6,171
Robotics Division							
Orders received	€ mio	429.6	385.3	338.4	382.3	434.9	464.4
Sales revenues	€ mio	417.7	420.5	323.6	373.3	412.9	474.4
EBIT	€ mio	48.3	43.9	-22.8	22.4	33.6	42
in% of sales	%	11.6	10.4	-7	6	8.1	8.9
in% of capital employed	%	53.8	38.6	-22.1	24.3	34.6	37.2
Capital employed	€ mio.	89.8	113.6	103.3	92.2	97.1	112.9
Employees		1,834	2,044	1,936	1,838	2,023	2,261
Systems Division							
Orders received	€ mio	651.7	780.4	778.2	847.8	937.7	854.9
Sales revenues	€ mio	734.6	715.9	791.2	832.8	900	837.5
EBIT	€ mio	20.2	35.1	-14.4	10	37.2	26.8
in% of sales	%	2.7	4.9	-1.8	1.2	4.1	3.2
in% of capital employed	%	11.1	21	-9.7	9.9	51	20.2
Capital employed	€ mio.	181.9	167.1	148.7	101	73	132.7
Employees		3,194	3,275	3,422	3,620	3,582	3,781

Source: KUKA

The financial investor

In the case of KUKA a large number of financial investors have invested in the company between 2003 and 2008. However, the restructuring process since 2003 is closely connected to the investment of Guy Wyser-Pratte and his company.

Wyser-Pratte Management was founded in 1991 by Guy Wyser-Pratte and is based in New York City. Currently approximated \$ 150 million in assets are managed by the firm in mutual funds. The firm concentrates on investing in undervalued companies and follows an active investor strategy. Over several years Wyser-Pratte has focused on investing in several European companies.

Wyser-Pratte became first known to a general public in Germany during the hostile takeover of the German telecommunication company Mannesmann by the British company Vodafone in 2000. His investment company was perceived as one of the driving forces in this deal. A year later Wyser-Pratte became a (minority) shareholder of the German defence company Rheinmetall Group and tried to exert pressure on the management to initiate a rigorous restructuring program.

Through these activities Wyser-Pratte built up an image as a shareholder activist who tries to influence with a comparatively low amount of capital invested and a minority of shares the strategy of the companies in which he is invested. He systematically searches for undervalued companies in which he can invest. After becoming a shareholder he uses public pressure and a press campaign to form a coalition with other investor to put pressure on management to change the company's strategy and increase share price through strategies like concentration on core business or selling parts of the business. In the German press he was quoted with the phrase "wake up and smell the napalm" which was a threat to management to accept a fight with the shareholders over the most successful strategy for increasing the company's value.

With a similar activist investor strategy Wyser-Pratte invested in several other German companies, as the following list shows:

- Rheinmetall (2001): Wyser-Pratte bought 7% of Rheinmetall's shares in February 2001 and tried to force the management to concentrate Rheinmetall completely on defence technology. However, the majority shareholder, the Röchling family, did not follow this strategy and finally bought Wyser-Pratte's shares after 8 months. During this time the share price almost doubled and Wyser-Pratte realized a profit of 15 Mio. DM. (Handelsblatt 11.03.2003)
- Babcock Borsig AG (2001): Wyser-Pratte invested in the former Babcock holding. However, the company became insolvent and Wyser-Pratte was not successful in his attempt to change the company strategy. He suffered a serious loss with this investment.
- Mobilcom (2001-2002): For a short time Wyser-Pratte was invested in Mobilcom. He favoured a complete take over of Mobilcom by France Telecom, which however was not achieved. In 2002 he sold his Mobilcom shares.
- Vossloh (June 2006-October 2006): In June 2006 Wyser-Pratte bought 3% of the technology holding Vossloh. This was accompanied by interviews to the press in which he announced his intention to help the management make the company more profitable. However, after a short period in which the share price did not rise, Wyser-Pratte sold his shares in October 2006.
- Balda (March 2007-March 2008): Wyser-Pratte bought 5% of the shares in March 2007 from the mobile phone supplier Balda. He held these share for one year and finally sold them early in 2008. (Handelsblatt 16.03.09)
- CeWe Color (since March 2007): At CeWe Color Wyser-Pratte first bought 3.3% of the shares, which he later increased to 5%. Together with other US hedge funds he fought against management without much success to make an extraordinary share buyback and replace the management. In January 2008 he reduced his shares to

1.14%. (Handelsblatt 08.01.2008). Shortly after he sued management for not correctly counting the votes at the annual meeting (Handelsblatt 27.04.09).

- TUI (since September 2007): At TUI Wyser-Pratte bought 1% of the shares in September 2007. It was the first time that he invested in a large DAX 30 company. He announced in the press that he would try to dismiss the CEO Frenzel. However, he failed.

The list shows how active Wyser-Pratte was in Germany for some time. In all cases he tried to use an activist shareholder strategy. In most cases several other funds followed him and invested in the same companies. Most of them held their shares short term (i.e. an investment of between 5 and 10 months).

In contrast with several other investments, Wyser-Pratte's investment in KUKA turned out to be not short-term but continued now for more than five years. When asked about KUKA Wyser-Pratte says that he believes in the mid term potential of the company and sees that his strategic vision for the company still has not been completely implemented.

9.4 The transaction

When Guy Wyser-Pratte 2003 invested in the former IWKA the company had structural characteristics which typically are a precondition for investments by activist shareholders. The company had a solid production structure with growth potential in several markets. It was not very profitable but its financial had been stable for years. At the same time it was undervalued on the stock markets and most shares were in free float, which makes the acquisition of shares easier. Additionally IWKA had a broad diversified company structure with one high potential branch, i.e. the robotics section. Such structures are very interesting for investors due to the potential for restructuring, concentration on the most valuable company divisions and other strategies which could create some short-term gains.

After the entry of Wyser-Pratte in 2003 numerous other private equity and hedge funds also invested in KUKA shares. Between 2004 and 2009 the company's shareholder structure lists 19 different investors which for some time were engaged in KUKA/IWKA with more than 3% of the shares. This had consequences for the regional distribution of shareholders. While in the 1990s more than 50% of IWKA shares were owned by German investors, after 2000 more and more foreign shareholders invested in the IWKA/KUKA. In this way KUKA is also an example of the dissolution of the so called "Deutschland AG", i.e. dense network of cross-shareholdings and interlocking directorates between German companies.

Financial investors at KUKA/IWKA

Overview financial investors at KUKA / IWKA	
Wyser-Pratte Management Co.: <ul style="list-style-type: none"> Entry on 27.10.2003 with a 5% stake Increase on 17.10.2005 to 7% Today WPM hold a 9,7% stake 	Massachusetts Mutual Life Insurance Company (MassMutual) (Hedgefonds) <ul style="list-style-type: none"> Entry on 02.06.2006 with a 5,18% stake Divestment in 2007 / under 3% Reentry on 20.01.2009 with a 4,87% stake Reduction on 23.02.2009 to 2,9%
The Capital Group International Inc.: <ul style="list-style-type: none"> Entry on 13.09.2004 with a 4,8% stake Divestment in 2005 / under 3% 	Cominvest Asset Management GmbH <ul style="list-style-type: none"> Entry on 07.02.2007 with a 3,09% stake Reduction on 22.08.2007 to 2,96% Divestment in 2008 / under 3%
Schroders plc: (Hedgefonds) <ul style="list-style-type: none"> Entry on 29.09.2004 with a 5,05% stake Divestment in 2005 / under 3% Increase / Reentry on 27.09.2006 to 4,96% Divestment in 2007 / under 3% 	Union Investment <ul style="list-style-type: none"> Entry on 13.04.2007 with a 3,03% stake Reduction on 09.10.2007 to 2,5% Divestment in 2008 / under 3%
K Capital Partners: (Hedgefonds) <ul style="list-style-type: none"> Entry on 06.05.2005 with a 5,29% stake Reducing on 02.01.2006 to 4% Divestment in 2007 / under 3% 	UBS AG <ul style="list-style-type: none"> Entry on 06.08.2007 with a 3,42% stake Reduction on 21.08.2007 to 1,36% Increase on 20.12.2007 to 2,57% Divestment in 2008 / under 3%
FMR Corp. (belongs to Fidelity Management – Hedgefonds activities) <ul style="list-style-type: none"> Entry on 04.10.2005 with a 5,61% stake Reducing on 02.08.2006 to 4,93% Increase on 12.10.2007 to 4,96% Increase on 16.10.2007 to 5,18% Reduction on 17.10.2007 to 4,89% Reduction on 29.10.2007 to 2,76% Divestment in 2008 Ausstieg / under 3% 	JP Morgan Asset Management Holdings <ul style="list-style-type: none"> Entry on 22.08.2007 with a 3,17% stake Increase on 12.11.2007 to 5,17% Reduction on 22.11.2007 to 4,67% Reduction on 24.01.2008 to 2,72% Divestment in 2009 / under 3%
Fidelity Management & Research Company (Hedgefonds activities) <ul style="list-style-type: none"> Entry on 12.10.2006 with a 5,64% stake Reduction on 12.10.2007 to 4,72% Reduction on 30.10.2007 to 2,88% Divestment in 2008 / under 3% 	Artemis Investment Management Lmt. (Hedgefonds) <ul style="list-style-type: none"> Entry on 31.10.2007 with a 4,86% stake Reduction on 18.12.2007 to 4,14% Divestment in 2008
Hermes Focus Asset Management Europe (Hedgefonds) <ul style="list-style-type: none"> Entry on 10.10.2005 with a 4,98% stake Divestment in 2006 / under 3% 	Morgan Stanley Investment Management <ul style="list-style-type: none"> Entry on 04.04.2008 with a 2,99% stake Divestment in 2009 / under 3%
Oppenheimer Funds Inc. (MassMutual) (see MassMutual) <ul style="list-style-type: none"> Entry on 17.03.2006 with a 5,13% stake Divestment in 2007 / under 3% Reentry on 20.01.2009 with a 4,87% stake Reduction on 23.02.2009 to 2,9% 	ODDO Asset Management (Hedgefonds) <ul style="list-style-type: none"> Entry on 17.04.2008 with a 4,48% stake Divestment in 2009
	Oppenheim Asset Management Services (belongs to MassMutual – Hedgefonds) <ul style="list-style-type: none"> Entry on 24.09.2008 with a 3,35% stake Increase on 29.09.2008 to 5,17% Today Oppenheim hold a 5,17% stake

Source: KUKA

Strategy of Wyser-Pratte and other investors

The KUKA/IWKA case shows the possible influence of an active investor as a catalyst for restructuring and for further investments by hedge funds and other institutional investors. In the literature an investor like Wyser-Pratte is sometimes seen as the “alpha wolf” who attracts other investors. In this case investors like K Capital Partners or Hermes support his active investor approach due to potential short-term gains from such a strategy. Both gain from this type of cooperation. The active investor needs other supportive investors to have significant influence at the annual meeting in favour of an active approach. Hedge funds can follow an opportunistic investment approach with a comparatively small share of stakes, relatively short investment periods and the potential of high returns. Wyser-Pratte is still invested in KUKA. He emphasizes that he follows a long-term strategy with KUKA. However, the current financial crisis has affected the economic perspectives for KUKA very negatively and the share price currently is very low, which makes an exit for investors very unattractive.

9.5 Consequences for core business

The KUKA/IWKA case is an example how an active investor together with other institutional investors can speed up industrial change in the affected company. In the KUKA case the whole company structure changed. After the entry of Wyser-Pratte and other investors the company focused on the high potential robotics division. Less profitable divisions like the packaging section were sold. In the period between 2004 to 2007 KUKA sold off sections with a total of more than 7,800 employees, moved their headquarters to Augsburg (where the robotics & systems section is located) and renamed the company after the robotics & systems section KUKA. Additionally, under the pressure of activist share holders, several changes in management took place and two CEOs resigned. Due to the disposals mentioned above the company reduced the number of employees from 12,859 in 2000 to 6,000 today.

Major cutbacks were caused in 2005 by the sale of six subsidiaries which accounted for more than 3,600 workers. The sale of another four subsidiaries in 2006 accounted for more than 1,400 employees. Finally, the biggest single reduction was caused by the sale of the packaging division with its 2,500 employees. Nevertheless most of the workers were not dismissed but rather transferred to new owners, although it is not clear how the companies that were sold developed under the new owners and to what extent there was continuity in the workforce after the sales.

This development is in line with the demands of Wyser-Pratte and other institutional investors. For them the robotics section was from the beginning the main object of interest.

IWKA disinvestments 2004-2007

IWKA AG Desinvestments 2004-2007						
Gesellschaft	Umsatz Mio EUR	Mitarbeiter	verkauft am	wirksam zum	Käufer	Käufertyp
Marcon Ing.gesellschaft	16	150	25.06.2004	01.01.2004	Management	MBO
Bopp & Reuther Messtechnik			30.06.2004	01.01.2004	Management	MBO
Inex Vision/ USA	10	80	15.10.2004	2004	Asset Deal	-
2004	26	230				
Heinrichs Messtechnik	6	70	02.07.2004	01.01.2005	Management	MBO
VAG Armaturen	74	700	10.12.2004	01.01.2005	EQUITA	Private Equity
RMG-Gruppe	100	970	23.12.2004	01.01.2005	TRITON	Private Equity
EX-CELL-O-Gruppe	160	650	29.12.2005	31.12.2005	MAXCOR/USA	Industrieller Investor
BKT-Gruppe	150	1000	22.12.2005	01.01.2006	Odewald & Cie	Private Equity
B&R Sicherheitsarmaturen	41	250	22.02.2006	01.01.2006	Tequity	Private Equity
2005	531	3640				
JW. Fröhlich	48	260	22.06.2006	30.06.2006	Management	MBO (Vorbesitzer)
Hassia Redakron	15	70	08.09.2006	01.12.2006	Piltz mbH	Industrieller Investor
ARO-Gruppe/ Frankreich	100	600	11.12.2006	11.12.2006	Langley/ ErB	Industrieller Investor
Boehringer-Gruppe	140	520	23.11.2006	21.12.2006	MAXCOR/USA	Industrieller Investor
2006	303	1450				
Geschäftsbereich Verpackungstechnik	404	2500	19.04.2007	19.04.2007	Odewald & Cie	Private Equity
Desinvestments 2004-2007	1264	7820				

Source: KUKA

Regarding divestments the KUKA case illustrates the importance of private equity in the German M&A market. Most of the parts sold by KUKA were bought by other private equity investors. Between 2004 and 2006 sufficient risk-oriented financing for such deals was available. The restructuring of KUKA was possible only due to high liquidity in the M&A market. Thus the interconnections between an active investor, hedge funds and private equity reinforce the influence of institutional investors on industrial change in this case.

As far as work organisation and internal processes are concerned the activities of institutional investors had no measurable influence on decisions and conflicts at KUKA.⁵¹ During the restructuring process employee representatives had no direct contact with the institutional investors. They were involved through their representatives in the supervisory board. But none of the investors sought direct contacts with the employee representatives. However, the general logic of the restructuring strategy was shared by the employee representatives and the trade union. They were relatively successful in making arrangements with the new owners to guarantee job security at the divisions of IWKA/ KUKA which were sold.

9.6 Economic development of the company and employment

From 1999 to 2004 KUKA constantly increased its net income from € 31.4 million in 1999 to € 48.5 million in 2004. The business years 2005 and 2006 were years of transition for KUKA AG. Whereas in 2005 the company implemented a deep-seated internal restructuring programme that encompassed all of the groups division, the years 2005 and 2006 were marked by several divestitures. In 2005/2006 KUKA sold ten subsidiaries with a total turnover of € 834 million. These actions affected the annual results. In

⁵¹ This observation was confirmed by representatives of the trade union as well as the management.

2005 KUKA had a net loss of € 147.5 million, in 2006 the net loss was reduced to € 69.4 million. Although the company sold its packaging division, which accounted for a turnover of € 404 million, in 2007 KUKA had a net income of € 117.9 million in that year. In 2008 net income decreased to € 30.6 million. This slump was mainly caused by the financial crisis and its severe impact on the automobile and automotive supplier industry.

KUKA Key Financial and Employment Figures, 1999-2008

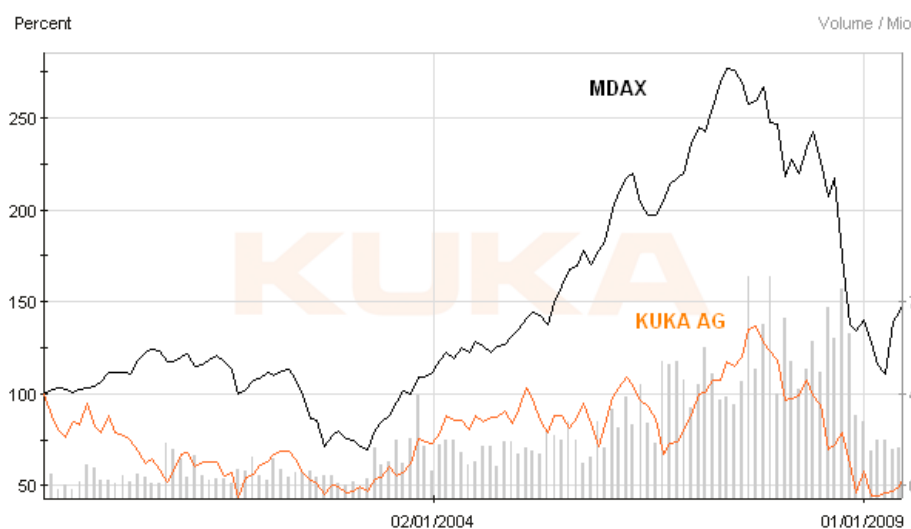
KUKA Group	Orders received (€ mio)	Sales revenues (€ mio)	EBIT (€ mio)	in% of sales	Net income / loss for year (€ mio)	Employees
1999	1.815	1.844	69.8	3.8	31.4	13,312
2000	2.189	2.220	50.8	2.3	31.0	12,859
2001	2.280	2.290	68.9	3.0	31.2	12,823
2002	2.361	2.312	73.4	3.2	22.5	13,089
2003	2.304	2.287	81.1	3.5	23.4	13,231
2004	2.340	2.352	111.9	4.8	48.8	13,209
2005	1.641	1.613	-30.7	-1.9	-147.5	8,974
2006	1.620	1.566	33.7	2.2	-69.4	8,123
2007	1.344	1.286	70.4	5.5	117.9	5,732
2008	1.280	1.266	52.0	4.1	30.6	6,171

Source: KUKA

KUKA and the capital markets

KUKA shares are included in the German mid-cap share index MDAX, which comprises 50 medium-sized German listed companies. KUKA shares are traded on all German stock exchanges and on the electronic trading platform Xetra. In comparison to the MDAX, KUKA shares have underperformed over the last ten years.

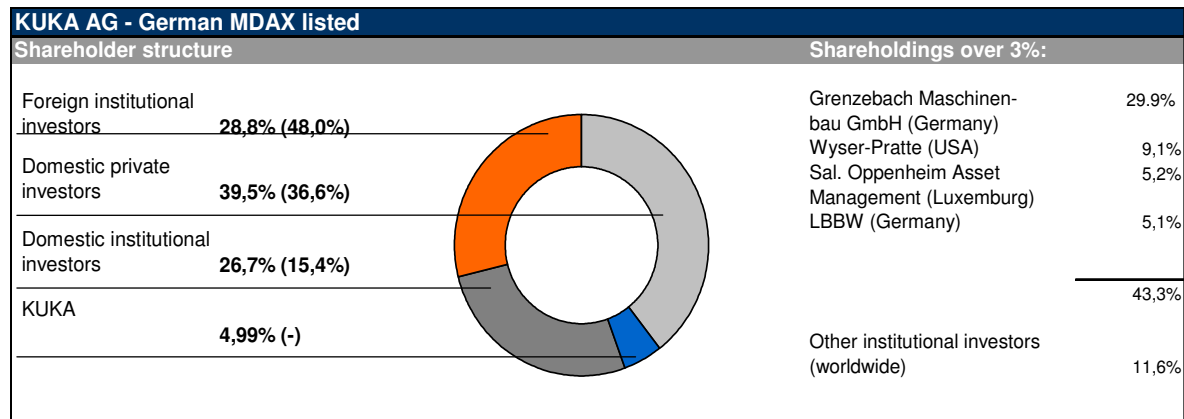
Development of the KUKA share



Source: KUKA price development from 14/06/1999 to 11/06/2009, company's homepage

Regarding the shareholder structure most of the KUKA shares are owned by international institutional investors (48% in February 2009). The remaining shares are controlled by German private investors (37%) and German institutional investors (15%). The shareholder structure of KUKA has changed over the last ten years from mainly German-based to a shareholder structure which has a higher proportion of foreign investors. With the investment of the industrial company Grenzebach (which today hold 29.9% of the shares) this development has been reversed to a certain extent.

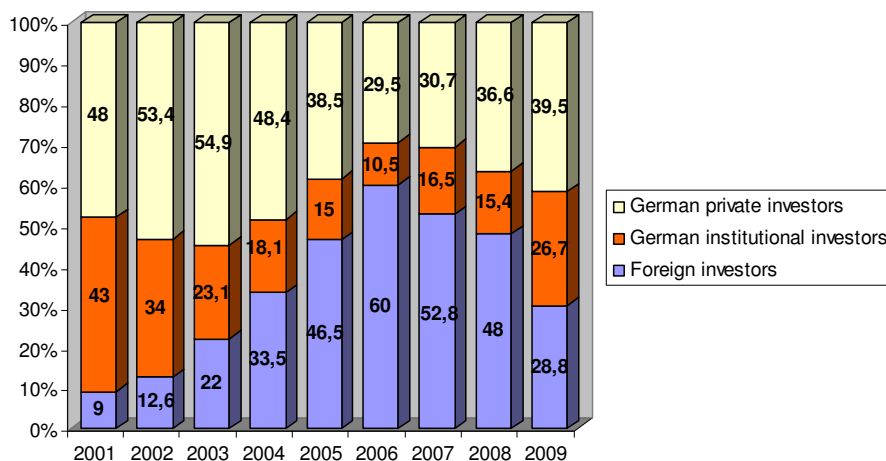
KUKA shareholder structure



Source: KUKA

KUKA however always tried to increase interest in KUKA shares among foreign investors. The company has held discussions with institutional investors and presented the company in leading European financial centres (i.e. "road shows"). As a result the share of foreign investors in KUKA has increased from 9% in 2001 to 28.8% in 2009.

KUKA AG shareholder structure



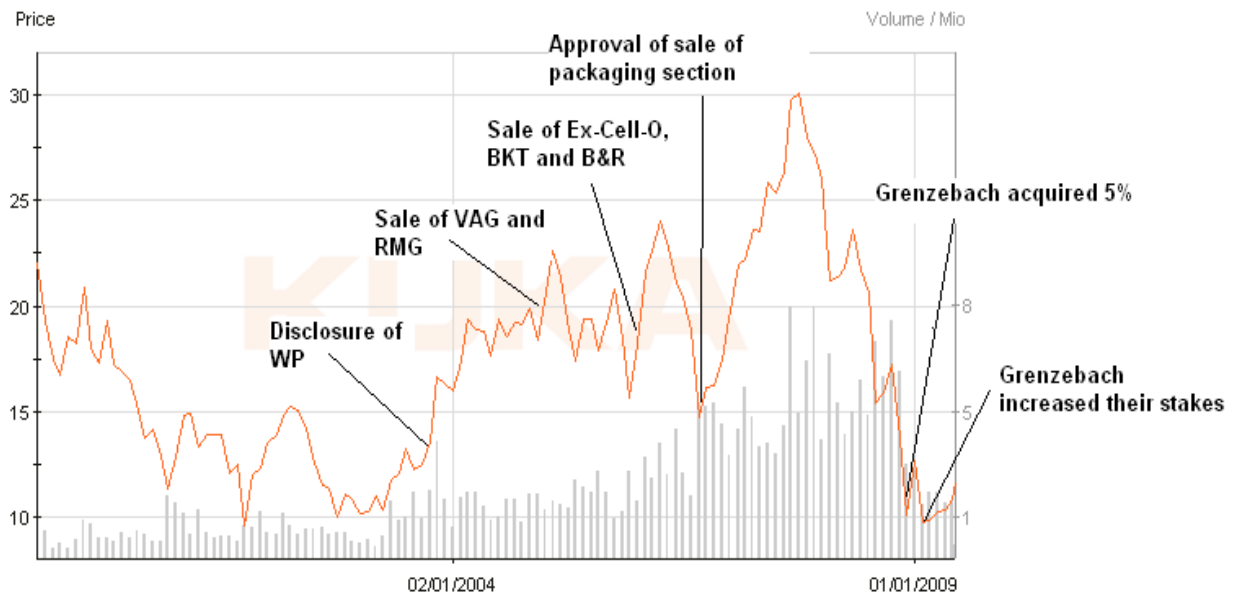
Source: KUKA AG annual reports 2001 – 2008

In terms of KUKA's stock market performance, the KUKA share price clearly was influenced by investment activities, restructuring measures and changes in the executive board. After Wyser-Pratte Management disclosed the acquisition of a 5% stake in KUKA the share price rose more than 5%. In 2004 KUKA started to sell major parts of the company and focus more on the innovative robotics section. After the divestment of the process technology section, the fittings section (VAG) and the RMG subsidiary in 2004 KUKA's share price rose more than 28% in seven months.

Similar results occurred after further divestments in late 2005 and early 2006. From 30th November 2005 to 31st March 2006 KUKA's share price rose more than 53%. After severe disputes between management and investors, particularly Wyser-Pratte, KUKA management approved the sale of the packaging division in September 2006, which was finally sold in April 2007.

These developments led to a sharp increase of the KUKA share price of more than 75% between September 2006 and June 2007. In 2008 the financial market crisis and the economic slump were also reflected in the share price on the stock market. Price drops in the double-digit percentage range were reported in all major industrial countries. The two leading German indices suffered a similar setback, with the DAX (largest 30 listed companies) and MDAX declining 40.4% and 43.2% respectively over the course of the year. As a company which is closely connected with the automobile branch and which is highly dependent on exports, KUKA's stock market price slumped more than 62% within one year. In recent times the investment activities of the German Grenzebach Group attenuated this development and led to a gradual increase in the KUKA share price.

KUKA share development in context



Source: Own

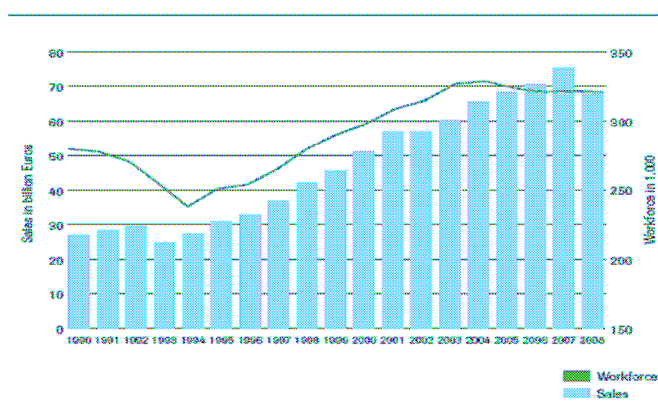
9.7 Comparison of company development with branch performance

Almost 70% of KUKA sales are connected with the automotive industry, thus the following sector analysis deals mainly with the automotive supplier industry. The German automotive supplier branch showed a steady growth in sales revenues since the mid-1990s of between 6% and 9% per annum. This growth was mainly caused by export sales, which became increasingly important in the last years. From 2003 to 2007 foreign sales increased by 15%. Domestic sales however still account for over 55% of total turnover in 2007. With the economic and financial crisis this positive development was drastically interrupted. Motor vehicles sales slumped globally, which caused massive income losses for the automotive supplier industry as well. German automobile manufacturers and their suppliers faced the worst economic situation since the last crisis in 1993. New car registrations in Europe and the US decreased, although current government actions like the so called "Abwrackprämie" (scrapping bonus) attenuated this trend somewhat. According to estimates the automobile supplier industry will experience a sales decline of up to 20% in comparison to the previous year.⁵²

⁵² IKB Deutsche Industrie Bank: Branchenbericht Automobilzulieferer, December 2008.

Sales and employment in the automotive supply industry

Sales and employment in the automotive supply industry



Source: VDA Annual Report 2008

To a lesser degree KUKA is involved in the mechanical and plant engineering sector. In the last ten years this sector was less stable than the automobile industry. In line with the general economic downturn in Germany at the beginning of the decade, the mechanical engineering sector showed no significant growth in the years 2001 to 2003. Comparable to the automotive sector exports had a stabilizing effect on the industry. Export growth also was the primary driver of the economic upswing in 2004. With the economic recovery the mechanical engineering sector saw a significant rise in demand. In 2005 the world economy as well as the German economy continued to expand. German growth in 2005 was also mainly supported by a high export rate. Germany once again had a record exports. Accordingly the mechanical engineering sector had a good year in 2005, with orders received at an historic high. This positive development continued in 2006 and 2007. In the outstanding 2007 business year, the German mechanical plant and engineering sector was able to increase manufacturing by 5% compared to the year prior.

However, toward the end of 2007, the economical climate deteriorated significantly, primary because of the beginning of the real estate crisis in the US.. This initial downswing was continued in 2008. Orders received, which are a leading indicator of future capacity utilization for companies, were already down 7% in 2008 compared to a year earlier. According to VDMA, the German Engineering Federation, the 29% year-over-year drop during the fourth quarter makes it the weakest quarter since 1958. The decline was the same for both the domestic and export business.⁵³

In Germany the real GDP growth rate was down by 50%, from 2.5% in 2007 to 1.3% in 2008. The forecast for 2009 assumes a real GDP growth rate of -5.2%.

Germany – main economic indicators

	2003	2004	2005	2006	2007	2008
Real GDP growth rate	-0.2	1.2	0.8	3.0	2.5	1.3
Employment rate in %	65.0	65.0	66.0	67.5	69.4	70.7
Unemployment rate in %	9.3	9.8	10.7	9.8	8.4	7.3

Source: Eurostat

A comparison between these sectoral developments and KUKA is not easy because the severe restructuring actions distort the economic development of KUKA. Nevertheless some findings can be reported. The beginning of this decade was for the German econ-

⁵³ See KUKA Annual Report 2008, p. 35.

omy in general and for KUKA especially a period of only slight economic growth. Particularly the years 2002 and 2003 meant for KUKA a decrease in net income and only a moderate increase in orders received. With the general economic upswing in 2004 KUKA was able to increase its net income by more than 50%, although orders received stagnated. As mentioned above, the years 2005 and 2006 were marked by significant restructuring actions, which resulted initially in quite negative financial performance. In line with the positive economic performance of the automobile sector and the mechanical engineering sector in 2007, this year was the most successful year for KUKA in the past decade, with an increase in net income by more than 200%. As was the case for the whole economy in 2008, KUKA was hit hard by the current economic crisis. At year-end net income had decreased by more than 70%.

In comparison with the general export rates of German automobile and mechanical engineering industries KUKA always showed a higher export orientation. Since 1999 the share of exports in sales revenues was quite constant at around 64%.

Regarding employment developments, a comparison with the branch development is difficult due to the above mentioned restructuring actions. While the supply industry in general constantly increased its workforce in the last decade (with a slow down in the last three years), KUKA steadily reduced its employment figures from 13,312 in 1999 to 5,732 in 2008.

9.8 Future perspectives for KUKA and exit strategies for financial investors

As is the case for many other companies closely linked to the automotive industry, KUKA faces a complicated economic situation in 2009 and 2010. Demand has drastically declined and it is unclear how long the current crisis will continue. The next months are secure as far as orders and financial resources are concerned. But the economic crisis will erode profitability. Therefore measures for cost cutting are seen as necessary.

Outlook for 2009
KUKA starting point
<ul style="list-style-type: none"> - Solid key figures in 2008 - Financing secured - Current order backlog provides level of activity for five months
Effects of the economic crisis
<ul style="list-style-type: none"> - Deteriorating economic crisis will substantially reduce overall customer demand - Since the beginning of 2009, KUKA orders received are down accordingly <ul style="list-style-type: none"> - Automotive already started in 2008 - General industry noticeable since beginning of 2009 - Impact on cash flow development
KUKA action plan
<ul style="list-style-type: none"> - Implementation of detailed measures to cut costs - Focus on liquidity - Active reduction of exposure
KUKA is positioned to compete successfully in the current difficult market environment

Source: From company presentation 2009

However, after the crisis period, management sees new and extended chances for profitable growth. The basis for this is the securing of the automotive business and an expansion strategy in growth segments like advanced robotics.

As KUKA is a listed company, exits for institutional investors are always possible. However, seeing the actual economic situation and that the main field of activity of KUKA is linked to the automotive industry, it seems not very realistic to predict that KUKA's share price will outperform. A decisive question is how the new core investor Grenzbach will act and in which way they will influence the strategic development of KUKA.

9.9 Summary: lessons to be learned from this case study

KUKA is an example for a continuous adaption process of a company to a fast changing economy. Since the early 1990s the company passed through several phases of change. By 2003 (when Wyser-Pratte invested in IWKA) the company had a promising portfolio of products and activities in different branches, but was not very profitable and also undervalued on the stock market.

With pressure from an activist shareholder it was possible to force a comparatively fast restructuring process in which several activities of KUKA were sold to other investors. The stock market reacted to these changes and this opened up chances for other investors like hedge funds. Therefore KUKA is a good example for an activist investment strategy combined with hedge fund investment.

It also shows the catalytic effect active institutional investors can have on industrial change. Before the active investor Wyser-Pratte invested in IWKA the British pension fund Hermes had larger shares in IWKA but never actively influenced the company's strategy. For some time this strategy of stock price based value creation worked. The share price of KUKA grew by 200% between 2003 and the end of 2007. Only the actual economic crisis has changed this picture.

The case shows that the impact assessment on industrial restructuring cannot be limited to KUKA but also has to follow up on the development of all those divisions and companies which have been sold during the last years. It is therefore not possible to present an estimate of whether in total a net increase or decrease in the number jobs resulted.

The case of KUKA indicates some of the advantages but also possible disadvantages regarding the role of activist hedge funds. On the one hand the purchase of a minority stake by a well-known activist investor appears to have been the catalyst leading to a massive divestment program by a diversified holding company. The focusing on core activities by KUKA, which account for about one half of the employment of the former company IWKA, has supported an increase in profitability in the company. The new strategy also seems to have been supported by other investors and by management. The share price has not substantially outperformed other midcap (MDAX) companies in Germany.

Furthermore, an assessment of the full impact of restructuring would have to look at financial and employment developments in each of the parts of IWKA/KUKA that were sold off. Since these were sold off to private equity firms, benefits in productivity, etc. that potentially may have been realized through restructuring under private equity (and through integration with a strategic investor, to the extent that such exits were realized by private equity) would have to be counterbalanced against the possible negative effects (especially during the financial crisis) of the large debt burden that is typically built up in the case of private equity transactions.

10 Schefenacker AG /Germany: A case of HF investment

10.1 Schefenacker: Take over by Hedge Funds after high economic losses

Introduction: Why was the case selected?

Schefenacker AG is an interesting case because it shows an example of an old family owned middle sized company to achieve industrial growth in a highly competitive world market by buying another company. In this process of acquisition the Schefenacker AG used opportunities provided by financial market in financing the takeover of a competitor with credit. However, as we will see in the following case study, the company was

not able to earn enough money to pay the interest and had to use refinancing instruments offered by banks and hedge funds.

The case therefore illustrates first the risks of any globalisation strategy which is financed mainly by risk-oriented capital. Second it shows how refinancing mechanisms work as well as restructuring after the failure of an expansion strategy.

Finally, it is also an example for a very creative and successful attempt of employees and the local trade union to save as many jobs and parts of the old company after the failure of the old management and its strategy.

10.2 Profile of the company and the financial investor⁵⁴

The company Schefenacker

Before becoming insolvent Schefenacker was a leading supplier for the motor vehicles branch and a global player in producing automotive mirrors and tail lights as well as premium automotive sound systems. Key customers included Ford, Daimler Chrysler and GM. With a € 930 million turnover (2007) the automotive parts group had 7,900 employees in 33 locations worldwide. After a long history of slow but continuous growth as a family owned company in the German market, after 2000 the company was characterized by a fast growth process.

Until 2000 Schefenacker was a traditional family owned enterprise. The company Schefenacker was founded in 1935 in Esslingen by Alfred Schefenacker senior. In its early years Schefenacker produced ceiling lamps for the automotive branch, later tail lights (since 1938) and automotive mirrors (since 1950) sections were developed. After the death of Alfred Schefenacker Sr. in 1995 his son Alfred Schefenacker Jr. took over the business and started to follow a more aggressive strategy on the world market. In 2000 he bought out the British competitor Britax. With this deal Schefenacker became the world leader for producing automotive mirrors. The Britax deal was 100% financed through borrowing on the international financial markets.

Turnover and employment

Schefenacker AG		2001	2002	2003	2004	2005	2006
Sales	€ mio	1006.3	998.2	978.5	952.0	935.0	n.a.
Net profits	€ mio	-32.1	-147.1	-21.2	-181.9	-37.0	n.a.
Employees		n.a.	6,100	6,101	6,079	5,975	~ 6,100

Source: Schefenacker

The financing for this acquisition was structured in an unusual and risky manner. The loan was relatively short term (only five years) and was based on overly optimistic economic assumptions. Although at the beginning the Britax deal seemed quite promising, the acquisition fell short of Schefenackers expectations. Sales decreased and the newly acquired operations were not as profitable as expected. In contrary, Schefenacker realized high net losses between 2001 and 2005. In total in these 5 years the loss amounted to 419.3 Mio. Euro.

In the 2002 business year the relation between net indebtedness and adjusted EBITDA of 4.1 was still moderate. The adjusted EBITDA of € 82.1 million was spent on € 46.6 million in capital expenditures and € 29.8 million in interest. However, the interest payments became a burden and a potential threat to the general existence of the company. This problem was intensified by unfavourable exchange rates in the following years. The continuous loss had two consequences: Schefenacker needed fresh cash flow and could

⁵⁴ The case study is based on public available information and an interview with trade union representatives.

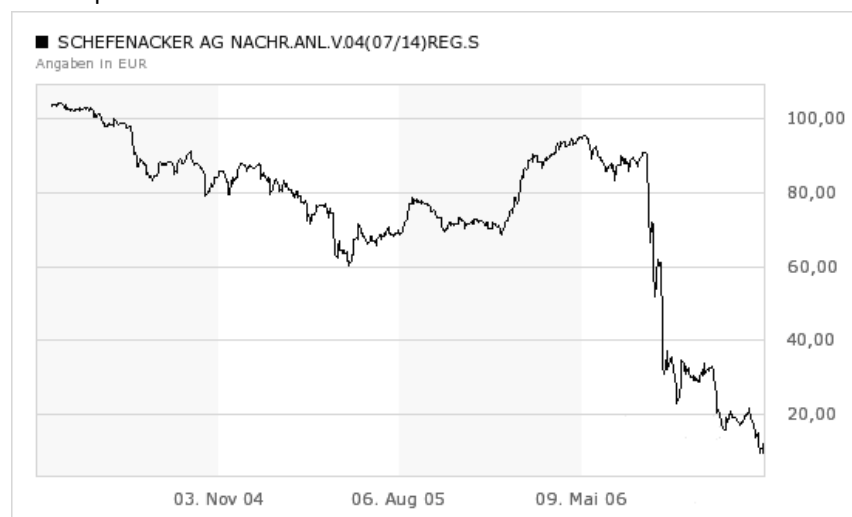
not fulfil its covenant breach of the loan facilities. As a consequence Schefenacker was not able to repay its loans, which amounted to € 450 million. More and more the creditor banks took control of the company. To avoid total asset stripping and a complete selling of the company, Schefenacker needed a quick debt restructuring. In 2004 Citigroup was assigned to issue another high-yield Schefenacker bond with a volume of € 200 million. With this step Schefenacker was able to shift the current liabilities to a ten years period. Nevertheless this was only a short-term recovering.

Performance of Schefenacker's bonds

By issuing new senior subordinated notes (€ 200 million bond in February 2004) more institutional and private investors got involved. Although Schefenacker's financial and economic problems were already apparent but at that time interest buying the bonds was high. Right from the start Schefenacker bonds had a very low "non-investment-grade" rating, i.e. for bonds that are in or approaching default. Nevertheless investors sensed the opportunity for high profits which resulted in a two and a half fold oversubscription Schefenacker's bonds and an issuance price of 104.5%. The bond was issued with a high interest rate of 9.5%.

However, Schefenackers poor economic performance continued and the bond lost value continuously over the first two and half years. However, after a slump to nearly 60% of par value the bond recovered in May 2006 to an annual high of around 92%. But in August 2006 Schefenacker presented disastrous financial figures for the second quarter of 2006. The result was a dramatic slump and only one week later the bond had a price of only around 30% of par value. As a reaction on the negative financial figures rating agencies like Standard & Poor's downgraded their rating for the bonds to "CCC-", which intensified the decrease in value and depressed Schefenacker's bonds to a trading price of 15%. Subsequently the bond lost more value until early 2007 when Schefenacker was reorganized into a PLC by British law. The main losers of this deal were the private bondholders. They held a 5% stake in debts and received an offer to transform their stakes into shares of the new Visiocorp plc. However at that moment these shares were almost worthless. Finally the private investors were compensated with €7.5 million, which was only a fraction of the originally invested amount.

Development of the Schefenacker share



Source: FAZFinance.net

Crisis and intervention of hedge funds

Schefenacker's difficult economic situation was also recognised by several hedge funds, which started to invest heavily in Schefenacker bonds. During the negotiations over debt restructuring in 2005 several creditor banks sold their debts to hedge funds, mainly to BlueBay and Davidson Kempner. Thus these hedge funds invested in Schefenacker through two channels, first indirectly with the buying of bonds and second directly by buying bank debts. Nevertheless the involvement of the hedge funds was in effect a last resort for Schefenacker to avoid a total shutdown. Furthermore the investment activities of the hedge funds led to more transparency and liquidity.

Schefenacker debts in June 2006 (in € million)

Revolving Credit Facility (Citigroup, etc.)	50
Second Lien (Davidson Kempner and BlueBay, etc.)	155
Subordinated loans (mainly free float)	200
Accrued PIK	2.6
Accrued Interest	2.1
Drawn bilateral Credit Lines	5.2
Overdraft of current Accounts	9.8
Capital Leases	3.5
Other	0.6
Total	428.8

Source: Schefenacker Press information 2006

In 2007 Schefenacker's management undertook a last and unusual step to save the company. To avoid insolvency under German law the company transferred the company's headquarters from Schwaikheim, Germany to Portchester, Great Britain. In late 2006 Schefenacker prepared this step with the incorporation of Visiocrp PLC as a shell company without operating business. The intention was that it would become the holding company for the Schefenacker Group. On 8 February 2007 Visiocrp PLC acquired the Schefenacker Group and with this acquisition Visiocrp commenced its operating business. In addition this new company was split up into two financially and legally independent companies in June 2007. The automotive mirror section, based in Portchester, continued operations under the name of Visiocrp PLC. The rear light section, based in Schwaikheim, was reorganised. This section was taken over by Schefenacker Vision Systems Germany GmbH (SVS), which was sold by the group to a third party trustee company. This new company was renamed Odelo GmbH on February 2008. This outsourcing process was managed in cooperation between the former Schefenacker management and the German metalworkers union IG Metal, thus resulting in a quite employee friendly job security plan for the German factory sides.

The Schefanacker successor companies

Visiocrp plc.		2007	2008	2009
Sales	€ mio	748.85	~ 700.00	n.a. ⁵⁵
Employees		5,026	~ 5,200	~ 5,300
Odelo GmbH		2007	2008	2009
Sales	€ mio	n.a.	n.a.	n.a.
Employees		1,010	~ 1,300	1,800

Source: Wilke, Maack and Partner

After separating the Group, Visiocrp continued operating only the mirror division. In spite of this focus on the presumably competitive mirror section, Visiocrp was not able to solve its financial problems. According to press information in late 2008 Visiocrp had

⁵⁵ Integrated into Motherson Sumi in March 2009

around € 300 million in debts. Since February 2009 the hedge funds owned Visiocrp. They started to negotiate with the Indian company Motherson Sumi over a sale of Visiocrp. On the 6th of March 2009 Motherson Sumi and Visiocrp agreed on an acquisition for € 26.5 million. Motherson Sumi already had a 49:51 joint venture with Visiocrp in India, called Visiocrp Motherson.

The former lighting section Odelo started an extensive restructuring programme agreed with employee representatives and labour unions, which aimed to achieve financial turnaround and a positive return by the year 2010.

Visiocrp plc. is a stock market listed company in Great Britain. With 23% in stakes Alfred Schefenacker Jr. is still one of the main shareholders of Visiocrp. In the last reported financial year 2006/2007 Visiocrp employed 5,026 employees in 12 countries. In Germany Visiocrp employed about 350 persons in Wolfsburg Hattorf, Schwaikheim and in the R&D section in Stuttgart. Since February 2009 Visiocrp negotiated with the Indian company Motherson Sumi over an acquisition. On 6th of March 2009 Motherson Sumi and Visiocrp agreed on an acquisition for €25 million and allotment of 5% shares for consideration with a face value of € 1.5 million. Motherson already had a 49:51 joint venture with Visiocrp in India, called Visiocrp Motherson. According to press information Visiocrp has around € 300 million in debt at the moment.

Odelo GmbH, the former Schefenacker Visions section, is still based in Schwaikheim and produces in Germany and Slovenia. In Schwaikheim, Kamp-Lintfort, Oberrot, Geislingen and two locations in Slovenia Odelo employed 1,800 persons.

The financial investor

As a result of the debt restructuring process the hedge funds Davidson Kempner and Blue Bay became the main investors. They together controlled around 70% of Schefenacker.

Davidson Kempner Capital Management LLC is a hedge fund management company which invests in public equity and fixed income markets across the globe. The firm makes its investments in distressed debt and stocks of companies that are undergoing corporate restructuring, including mergers, spin-offs, liquidations and recapitalizations. It also utilizes event-driven strategies including merger arbitrage, long/short, and convertible arbitrage strategy to select its investments. Davidson Kempner Capital Management was founded in 1990 and is based in New York.

The other hedge fund, BlueBay, was founded in 2001 and is based in London. The company is one of the largest independent managers of fixed income debt funds in Europe, with assets under management of approximately \$ 21 billion in 2008. According to company information the focus of BlueBay is on European financial markets. In 2008 BlueBay had \$ 16 billion under management in Europe, the only region where BlueBay makes direct investments. In Germany BlueBay is known because of their investment in the football club Borussia Dortmund. Since November 2006 BlueBay is traded on the main market on the London Stock Exchange (LSE).⁵⁶

10.3 The transaction

Due to the financial troubles of Schefenacker AG the two hedge funds were able to acquire majority control of the company in 2005. After the financial difficulties and continuous losses after the Britax takeover Schefenacker was in fact dependent on different creditor banks. During the debt restructuring process several banks sold their loans to BlueBay and Davidson Kempner, i.e. a so-called selling of "non performing loans". Additionally these hedge funds invested in Schefenacker bonds. At that time such transactions were quite new in Germany because the corporate bond markets were just emerging. Financial investors who followed so-called event-driven management strategies started to concentrate on "distressed debt" and companies with financial problems. For Schefenacker the restructuring actions resulted in a debt to equity swap, i.e. the hedge funds transformed company loans into company shares. Eventually they owned

⁵⁶ All attempts to do interviews with representatives of both funds on the Schefenacker case failed.

around 70% of Schefenacker, while the former sole owner Alfred Schefenacker Jr. retained around 25% as a minority shareholder. For Schefenacker this transaction was a last resort to avoid a total breakdown and asset stripping of the whole company.

Barclay Distressed Securities Index

Fund managers in this non-traditional strategy invest in the debt, equity or trade claims of companies in financial distress or already in default. The securities of companies in distressed or defaulted situations typically trade at substantial discounts to par value due to difficulties in analysing a proper value for such securities, lack of street coverage, or simply an inability on behalf of traditional investors to accurately value such claims or direct their legal interests during restructuring proceedings.

The following table shows average performance figures for these kinds of investments.

Year	2009	2008	2007	2006	2005
YTD	10.08%	-31.70%	6.91%	14.70%	7.87%

Strategy of the investors

For BlueBay and Davidson Kempner Schefenacker was a risky but interesting investment target. One can assume that, due to the financial pressure which affected the company as well as the banks, the debt was acquired at a relatively low price but offered extensive influence over the company's strategy. Schefenacker was a global leader in the production of automotive lights and mirrors and had a very strong position in the German and other automotive components markets.

A significant fact was the involvement of representatives of the automotive industry in the negotiations over debt relief, since the industry had a strong interest in the survival of the company. Schefenacker was at that moment the main supplier for automobile mirrors, which meant – as a German newspaper put it – “without mirrors, no cars”.

However, the transaction was highly risky due to the permanent loss of the company, the problematic financial situation and the expected expenses for restructuring measures. Comparing the two parts of the company one can see that the rear light section had more employees. But the mirror section had a higher potential from the hedge funds' point of view because there were potential buyers for this business.

Consequently BlueBay and Davidson Kempner concentrated on the mirror division. In late 2007 they split Schefenacker into two separate companies. First, the hedge funds tried to sell the lighting section. But in the end none of the potentially interested parties like Hella, Bosch or Magna agreed to a deal.

They were more successful with the mirror section. In March 2009 the investors finally sold the remaining mirror section Visiocorp to the Indian company Motherson Sumi Systems for around € 26.5 million.

The lighting section was transformed into an independent company (later called Odelo) which was sold to an industrial consortium in which companies from the German automotive industry are involved.

Consequences for core business

As a consequence of the poor economic performance between 2000 and 2003 since 2003 Schefenacker underwent several extensive restructuring attempts. As is typical for such situations the management changed several times and the company started negotiations with the trade unions on restructuring plans, which included wages cuts and mass layoffs of employees.

The most obvious results of the different attempts of the fast changing management were high additional cost in marketing and restructuring without achieving an economic turn-around.

As mentioned before one of the last steps was to relocate the company headquarters from Germany to Great Britain and to split up the firm into two independent companies. Although these actions already were carried out under pressure from the investors BlueBay and Davidson Kempner, the origins of the problems can be found in the Britax takeover in 2000 and the economic losses in the following years. As mentioned above, in the end the investment of the hedge funds was the only option for Schefenacker to avoid insolvency in 2005.

Chronology	
2000	Schefenacker takes over the British competitor Britax and becomes world market leader in the automotive mirrors branch. This deal was mainly debt financed, which subsequently caused severe financial problems.
2000 - 2003	High net losses in every year. In 2003 alone a net loss of 147 Mio. Euro, i.e. – 14.7% as % of all sales.
February 2004	To avoid a total break down Schefenacker was forced to acquire new liquidity and commissioned Citigroup to issue a € 200 million high-yield bond.
27.02.2006	Schefenacker is relocated from Esslingen to Schwaikheim.
12.10.2006	Schefenacker terminates its relationship with the CEO Hans-Joachim Lange. He is followed by Reiner Beutel, whose role is to undertake negotiations with the creditors. The main aim is a debt to equity swap with the support of a financial contribution by Schefenacker's owner Alfred Schefenacker Jr.
06.11.2006	As part of the restructuring process Schefenacker relocates its headquarters from Germany to Great Britain. With this step Schefenacker avoids insolvency under German law. Legally this step was prepared through the incorporation of a new company called Visiocrp PLC.
11.12.2006	CEO Reiner Beutel is dismissed. Stephen Taylor takes over running the business.
January 2007	Several banks sold their Schefenacker debts to British hedge funds. Additionally these funds acquired large positions in Schefenacker bonds. Finally the hedge funds Blue Bay and Davidson Kempner owned 70% of Schefenacker. The former main owner Alfred Schefenacker Jr. kept only a 25% stake in the company.
08.02.2007	The newly created Visiocrp PLC acquired the former Schefenacker Group.
04.06.2007	Stefaan Vansteenkiste, known as a specialist for restructurings, replaces the former CEO Taylor.
03.07.2007	Only one month later the CEO is changed again. The former BMW and Mercedes manager Ulrich Bruhnke takes over management.
29.06.2007	The former Schefenacker AG, now Visiocrp PLC, is split up into two financially and legally independent companies. The mirror section continues operations under the name Visiocrp, while the lightning section is reorganized under Schefenacker Vision Systems (SVS).
01.02.2008	The former Schefenacker lightning section SVS is renamed as Odelo GmbH
09.03.2009	Due to continuing financial problems Schefenacker's successor company Visiocrp Systems is sold to the Indian company Motherson Sumi for € 26.5 million.

After the debt to equity swap BlueBay and Davidson Kempner began to focus the company's strategy on the internationally more important mirror section, which finally led to the outsourcing of the lighting section in late 2007. This division henceforth operated as "Odelo Automotive Signal Lights" as a fully independent company in Schwaikheim, Germany. The three factory sites in Germany are involved in lighting, which account for more than thousand employees and were outsourced to an independent company. The owners of this company are OEM and German car manufacturers, who are dependent on the continuous production of signal lights.

During this outsourcing process the hedge funds were confronted with strong employee representatives which achieved quite good protection measures for the employees given the difficult business situation. In 2007 the unions were able to protect all of the three German factory sites in the lightning section, although the management and the investors planned to sell the factory site in Geißlingen.

In total 500 jobs were lost, but further extensive dismissals were avoided. During the outsourcing process of the lightning section the trade union IG Metall negotiated a collective agreement with employment guarantees lasting until 2012. Today the successor companies VisiCorp and Odelo together have almost as many employees as the former Schefenacker AG had.

10.4 Trade Union strategy: an example of innovative job security concept

Although the Schefenacker case was not very successful regarding the company's general economic development, it is at least an interesting case regarding the cooperation between the social partners.

Already in July 2005 the IG Metall negotiated a restructuring plan for the former Schefenacker lightning sections Schefenacker Visions, ULO and SVS. The main aim of this plan was the preservation of the company sites in Geislingen, Oberrot, Schwaikheim and Esslingen until at least 2010. In return the employee representatives supported the Schefenacker restructuring plan "Transition". This plan was initiated in October 2004 in collaboration with the international consulting company Mercer. Its goal was the restructuring of all the German production facilities as well as the Schefenacker locations in Selmer/USA, in Hungary (SAPU) and in Slovenia (SGA). The repositioning program was designed to further improve the profitability of the company and had five key points (see box below).

Although the plan included severe restructuring steps for all German factory sites, especially the closing of the Schefenacker site in Geislingen, IG Metall was able to prevent mass lay offs until 31 December 2010. Nevertheless it was quite clear that a long-term securing of all factory sites and the total workforce was not realistic due to the difficult financial situation.

Key points in the Schefenacker restructuring plan "Transition"

Locations – the management identified several opportunities for cost savings. This includes the transfers of production to lower cost countries, more efficiency in the supply chain network through a stronger focus of the different sites on specific products and technology. In 2005 a new production site in Slovenia started serial production of lighting products. Additionally Schefenacker installed injection moulding and plastic painting facilities at the Hungarian plant to improve vertical integration in their products.

Purchase and logistics – Schefenacker extended their cost reduction efforts to new areas. Significant progress has been achieved with vendor bundling and aggressive East Europe sourcing.

New product introduction – Schefenacker sought to improve its product development process to not only shorten time to market but also to reduce indirect costs.

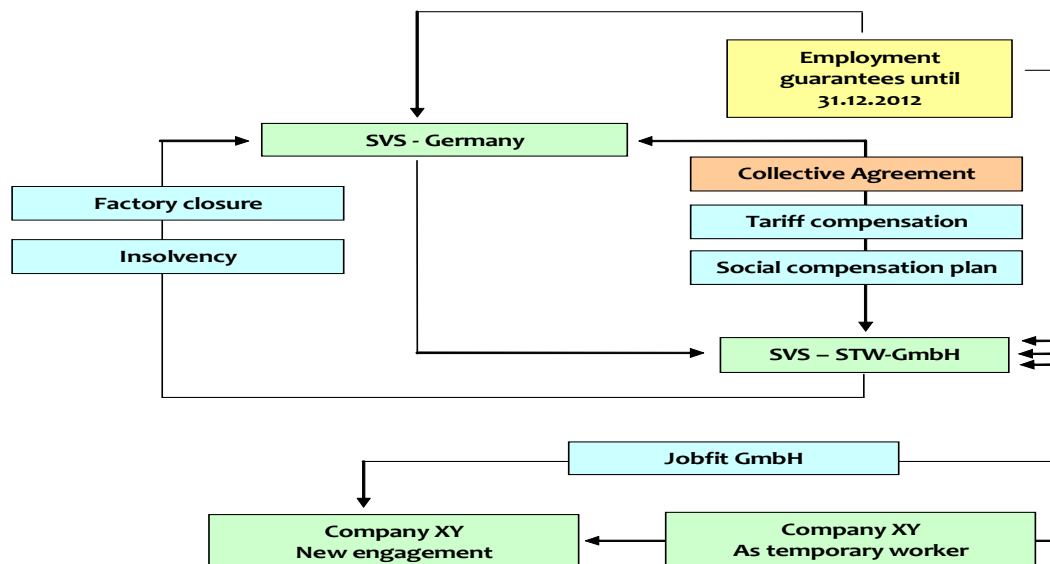
Organization – through further centralization and other organizational initiatives Schefenacker substantially reduced overhead cost and administrative effort.

Transparency – Schefenacker implemented additional controlling and reporting processes and tools to gain optimal transparency in business performance.

Two years later the already-mentioned split up of the former Schefenacker AG into the mirror section and the lightning section took place. This process was strongly influenced by German employee representatives IG Metall and the works councils. IG Metall and the management jointly developed an innovative model for the restructuring of the Schefenacker lightning section. The key focus of this plan was the creation of a subsidiary company called SVS-STW-GmbH. The SVS-STW-GmbH was constructed as a tempo-

rary employment agency and acted as a rescue company for all workers that were dismissed from the main company SVS. These workers were to be placed in other companies with the help of a personal management company called Jobfit GmbH. During the new engagement workers had the opportunity to suspend their contract with the SVS for up to two years. In case the new company went insolvent or the new factory closed down, the worker could return to SVS. For both SVS and SVS-STW, IG Metall negotiated employment guarantees until 31.12.2012. The employee representatives and management as well as the local media regarded this social plan as unique and innovative.

Structure of the social plan and the SVS-STW GmbH



Source: IG Metall Baden-Württemberg

Furthermore IG Metall was able negotiate income security for the SVS workers and a guaranty for all German production sides of the former Schefenacker AG. In total only 500 workers were dismissed, most of them at the Schwaikheim site. IG Metall was aware that employment cuts were not avoidable in general and that only a restructuring of the company would prevent a total breakdown of lightning section. According to IG Metall there was no alternative to this restructuring plan.

10.5 Comparison of company development with branch

In the case of Schefeacker a comparison with branch development trends is complicate. In general the German automobile supplier branch showed a steady growth in sales revenues since the mid-1990s of between 6% and 9% per annum. This growth was mainly caused by export sales, which became more and more important in the past few years, although domestic turnover still accounts for over 55% of total turnover in 2007. From 2003 to 2007 foreign sales increased by 15%.

However, due to its specific situation, Schefenacker could not participate in this overall positive trend. The internal problems, a management which was not able to organize an economic turn-around and the high financial debt from the acquisition of Britax forced Schefenacker into a dead end situation. After a fast growth process in 2000 by buying Britax Schefenacker became clearly a low-performer with negative economic results. The strong market position didn't help the company because Schefenacker never reached a profitable situation after the year 2000.

After the bankruptcy of the former company the two successor companies Odelo and Visiocrp are now facing a complicated situation which is very much influenced by the

overall economic crisis with a dramatic decline in demand for the automotive industry. It is unclear what this will mean for the successor companies.

10.6 Summary: lessons to be learned from this case study

The crisis and the subsequent restructuring process of Schefenacker AG originally was not triggered by activities of financial investors. It was a result of an excessively risky growth strategy of the owner and the management of Schefenacker, which was based on the assumption that the acquisition of Britax could be financed out of the profits earned on the market. Together with a low economic performance and the risk profile of a debt-financed takeover of Britax without sufficient capital from Schefenacker resulted in an economically dangerous situation for the group.

From this point on the Schefenacker case illustrates the mode and functioning of one of the business models of hedge funds. The investment, i.e. the acquisition of debt, was highly risky but on the other side offered the potential for outsized profits. Finally, after several internal attempts to restructure the company and make it more profitable the hedge funds searched a way out of the investment by stripping the company and selling the parts to other industrial investors. The hedge funds in this case were the last option for Schefenacker, since without these investors the company would already have failed in 2005. After a debt to equity swap the investors started a broad restructuring process which didn't protect Schefenacker as a whole but assured the survival of most of the company's parts under new ownership.

The strong position of the employee representatives in Schefenacker provides a good example of the influence of external factors on the outcome of such restructuring processes. In fact, in this case institutional investors like hedge funds adapted to national industrial relations and social practices and agreed to a political solution which saved most of the jobs at Odelo by using a transfer company. Although the hedge funds' investment strategy followed a classic restructuring model in the first phase, employee representatives had a quite influential position in the restructuring process and were able to avoid large scale dismissals and factory closings.

11 Cegelec /France: A case study of a SWF investment

11.1 Overview of PE, HF and SWF investments in France

France is the second most important country of the six countries studied in terms of private equity, both as a recipient of PE investment and also as headquarters for PE fund management. Although fundraising slowed substantially in 2007 (compared to 2006), PE investment activity continued to increase in that year and has roughly doubled in importance between 2003 and 2007. Seed investment has been very weak throughout the period, and there has been a marked shift in relative weight towards buyout activity (57% of investment in 2003 versus 85% in 2007).

Identified hedge fund equity investments in listed French companies were modest at the end of 2008, but this is likely an understatement of HF importance during the period due to underreporting and also the shift of many HF from long to short positions over the period.

Nineteen of the twenty top SWF positions in listed companies in France were accounted for by Norges Bank. One of the twenty positions was held by the Abu Dhabi Investment Co. (holdings of 7.7% of Vivendi shares outstanding).

11.2 Cegelec – from Private equity to Sovereign Wealth Fund

Introduction: why was the case study selected

Cegelec was chosen as an interesting case study for three main reasons. First, Cegelec has been controlled by equity investors since 2001. In 2001, its predecessor, Alstom Contracting, was acquired by its managers and employees in a LMBO (Leveraged Management Buy-Out) with the backing of two financial institutions, CDC IXIS Private Equity and Charterhouse. The company was renamed Cegelec. In 2006 Charterhouse Development Capital and CDC Enterprises Capital sold the company to the Private Equity group LBO France for about € 1.1 billion, including debt. Finally in 2008 the Sovereign Wealth Fund QD Real Estate Investment Company (Qatar Dia) bought Cegelec for € 1.6 billion. Qatar Dia (QD) is wholly controlled by Qatar's Sovereign Wealth Fund, Qatar Investment Authority (QIA).

Second, Cegelec is one of the European leaders in electrical engineering (see below for a description of the firm). Though France is its major location, Cegelec has historically had a presence in Belgium, the Netherlands, and Germany as well as in other European countries. Cegelec also has subsidiaries outside of Europe (Morocco, Algeria, Brazil, the Middle East and Asia). It has around 25,000 employees (around 19,000 of these in Europe). The construction sector has been one of the most important sectors for the Private Equity fund because of its strong growth in recent years and because of its weak capitalization. In France, as in Europe generally, Private Equity has taken an important place in the economy and in mergers and acquisitions, although investment activity slowed down when the financial crisis hit in 2007/8. Up to that point, credit provided by the banking system contributed to a sharp growth in the valuation of companies.

Third, as mentioned above, QD is a subsidiary of one of the world's largest SWFs and provides an interesting example of a strategic acquisition. As will be shown, this has implications for restructuring and employment.

11.3 Profile of the company and the financial investor⁵⁷

The company Cegelec

Cegelec is one of the European leaders in electrical engineering, specializing in integrated solutions and technological services. Cegelec designs, installs and maintains systems or sub-systems in industry, infrastructure and the service sector. It is an integrated international group providing technological services to companies, and public authorities. Cegelec provides technological services mainly in the field of energy and electricity, automation, information and communication technologies, HVAC (heating, ventilation and air conditioning) systems. Cegelec's core markets are infrastructure projects, the industrial sector, maintenance and buildings. The Group is present in some 30 countries, including Europe and other parts of the world, through a network of over 1,200 offices. In 2008 the group generated an annual turnover of around € 3 billion: 24% in the industrial sector, 30% in infrastructure, 19% in the service sector and 27% in maintenance.

Key figures of Cegelec 2008 in comparison to previous year

Key figures Cegelec 2008 (compared to 2007)	
EBIT: € 157 million (+12.7%)	Revenues: € 3 billion (+3.1%)
Orders: € 3.22 billion (+13.1%)	Free cash flow: € 213 million

Source: Cegelec

⁵⁷ The following analysis is based on publicly available material and company information. In addition interviews were done with Cegelec management and members of the European Works Council.

Core businesses and markets

Cegelec's activities are focused on five core business areas:

i) Energy and electricity. Electrical engineering forms the historical core of Cegelec's business activities, with power production, transmission and distribution accounting for 56 % of the Group's sales.

ii) Automation, instrumentation and control. Cegelec's know-how covers low voltage applications that fit closely with its traditional high voltage activities. Cegelec applies its expertise to automation and control systems (control, instrumentation, control rooms, fire detection and fire fighting systems, access control and building controls), helping customers to raise productivity and the quality of their production processes.

iii) Information and communication technologies. With the rise of new technologies, Cegelec has enhanced its offerings in the telecommunications and IT sectors.

iv) Heating, Ventilating, and Mechanics. Cegelec offers solutions for technical installations, for new buildings or rehabilitation projects, design of facilities capable of generating fresh air at a comfortable temperate. Cegelec offers a broad range of skills in mechanical engineering, including office design, repair teams and workshop organization.

v) Maintenance and services. Cegelec offers maintenance services covering electrical maintenance and instrumentation, maintenance of motors and rotating plants and maintenance of pipes and valves. Cegelec also offers global maintenance services.

The company operates in four major markets:

i) Infrastructure. Infrastructure projects account for about one third of Cegelec's annual revenue. Cegelec is a systems integrator providing services in five sectors: energy, transport, telecommunications, defence, household waste and water management.

ii) Manufacturing. Manufacturing is one of Cegelec's core markets, accounting for around 25 % of consolidated revenue. It was the company's first market, which had an important influence on the development of its corporate culture.

iii) Maintenance. Over the years Cegelec has become a major player in the maintenance market: Corrective maintenance, preventive maintenance (both on a systematic and a one-off basis), audits and maintenance plans, responding to on-call situations, etc. In all maintenance activities now account for nearly a third of the Group's sales.

iv) Construction. Cegelec is a global player here: expertise in air conditioning, electrical engineering, plumbing, fluids, building management services and automated systems, communication and networks, safety and tenant services. Cegelec is involved from the building's design phase and is in direct contact with the developers and building owners.

Organisation

The company's international headquarters are located in Brussels. Cegelec has set up a client-based organisation around five entities:

- CFB (France): domestic business in France and its overseas territories. Around 11,500 employees. CFB accounts for 50% of Group revenues.
- GSS (Global Systems & Services): global and industrial maintenance and large projects in France, Europe and beyond. Some projects are developed with local subsidiaries. Around 2,400 employees are based in France.
- CGB (Germany and Austria): business in these two countries, with around 1,900 employees.
- CBB (Cegelec Benelux Business): local business in Belgium (major operator) and Netherlands (newcomer), with around 2,200 employees

- CWB (Cegelec Worldwide Business): domestic business with major locations in Morocco, Brazil and the Middle East. It has three subsidiaries in Europe (Spain, Switzerland and Poland) and has around 1,000 employees.

The financial investor Qatari Diar

Since 2008 Cegelec has been controlled by the sovereign wealth fund, Qatari Diar, which is a wholly-owned subsidiary of the Qatar Investment Authority (QIA). QD is the real estate branch of QIA. Together with Barwa and Qinvest it is one of the instruments for Qatar's investment strategy. QIA is the sovereign wealth fund of Qatar, focussing on three asset classes: real estate, private equity and local and foreign investment funds. It was founded in 2003 to manage Qatar's financial surpluses from oil and natural gas. In order to minimize Qatar's reliance on energy prices, the fund predominantly invests in international markets and within Qatar outside the energy sector. In 2008 QIA ranked number 6 among oil-exporting sovereign funds worldwide in terms of its capital (\$ 62 billion)⁵⁸. The details of QIA assets are not publicly available, but it is believed that QIA recently has reduced its exposure to the US Dollar to 40% of assets and that the rest of the fund is in Euros (40%), in Pounds Sterling (20%) and in Asian currencies. The owner of the QIA is Qatar's royal family Al-Thani.

QIA is defined by the IMF as a stabilization fund or a raw materials fund (which represent two-thirds of SWF assets). Stabilization funds are endowed with revenues generated by the export of natural resources from the country and are for the purpose of protecting economies against changes in the price of raw materials, stabilizing budgetary revenues and accumulating wealth for future generations.

According to a November 2008 ranking, QIA is considered to be the number 9 SWF worldwide in terms of its capital (\$ 60 billion) thanks to an annual endowment equal to 10 % of oil revenues. The exact amount of QIA assets is a state secret. International rankings based on the transparency of SWFs (Standard Chartered 2007, Peterson Institute for International Economics 2007) rate the QIA as one of the "last in class".

QIA's Major Direct Foreign Investments (Public)

Company	Country	Ownership
Sainsbury J Plc- Underlying	UK	27.28%
London Stock Exchange	UK	15.1%
Imagination Technology Group	UK	11.4%
Epicure Qatar Equity Opportunities	UK	10.1%
Credit Suisse	Switzerland	ca. 10% (Qatar Holding)
Banyan Tree Holdings	Singapore	7.1%
Barclays Bank	UK	6.4%
Lagardere	France	6.09%
Fortress Investment Group LLC	US	

Source: Qatari Diar

Regarding investments, Qatar has engaged for several years now in a diversification strategy. Qatar's investment approach is considered by Standard Chartered to be one of the most strategic-oriented among the top 20 sovereign funds worldwide. Its investments include the following: US and European assets: 20% of the London Stock Exchange Group and 10% of the Swedish stock exchange (Nordic Exchange OMX), a major investment in Crédit Suisse, 5.1% stake in Lagardère, 25% stake in the UK's Sainsbury supermarket chain, and an objective of obtaining a 10% stake in EADS. Second, large investments in real estate and industrial projects: construction represents 40% of all investment projects, hydrocarbons and chemicals 45%, water and electricity 5 to 12%.

⁵⁸ ECB- Occasional Paper Series, No. 91 July 2008: <http://www.ecb.int/pub/pdf/scpops/ecbocp91.pdf> - p.10.

QIA's Major Direct Foreign Investments (Private)

Company	Country	Type	Ownership
Cegelec	France	Subsidiary	100% (owned by Qatari Diar)
BLC Bank-France	France	Subsidiary	100%
Chelsfield Partners LLP	UK	Real Estate	20%

Ssource: Sovereign Wealth Fund Institute

Although Qatar is one of the most liberal and most open countries among the Gulf Co-operation Council countries (e.g. Qatar was the first gulf state to engage in diplomatic relations with Israel), the country's prosperity is based on the exploitation of natural gas reserves and (arguably) also on the low cost of Asian migrant workers.

QD, the real estate branch of QIA, has a 45% stake in Barwa Real Estate Company. It has been in a joint venture with Barwa Suez since May 2008. 95% of its business will be generated in Qatar in the environmental sector: water treatment, desalination, clean gasses, collection and treatment of different types of waste;

The Chairman and Vice Chairman are the Prime Minister and the Minister of Finance of Qatar, who are members of the Emir's family. QD's investment strategy is aimed at making Qatari Dian one of the top "master developers" in the world. QD designs and performs colossal, all-encompassing real estate projects everywhere throughout the world (Cuba, Singapore, the UK), but mainly in Africa and the Middle East (Libya, Yemen, Syria, Sudan, Morocco).

QD has \$ 10 billion line of credit from QIA to invest in the next few years. It has been changing its strategy from a "sleeping partner" to a more coordinated medium-term strategy. Cegelec is its first operation of this size, however QD is also initiating various projects with different partners, taking either equity stakes or participating in ad hoc joint ventures. QD follows a development oriented strategy around infrastructure and services activities. Most of its partners are European. It may be linked with the political strategy of the country that builds relations with both the USA and the EU. In the infrastructure area it is involved in the construction of the bridge between Qatar and Barhein in partnership with Vinci (JV: QDVC) and of the railway network of Qatar with Deutsche Bahn; in services it is involved with Suez in two major projects in Qatar and in a large project with QDVC

Description of LBO France (2006)

LBO France was created in 1985 and in the following 20 years has acquired about 60 firms valued at € 8.7 billion. Cegelec was the biggest investment made by this Private Equity firm. Major acquisitions made in 2005 were Actarias (with about € 670 million in annual turnover) and Terreal and Wheelabrator (between € 350 and € 400 million in turnover). As is typical for Private Equity, LBO France has a 25% profit target for its operations.

11.4 The transaction

Situation of the company at the beginning of the transaction

LBO France bought up Cegelec in 2006, which at the time was valued at € 1.1 billion (including debt). This valuation was € 350 million greater than the 2001 figure even though the improvement in Cegelec's economic performance was very limited. The increased valuation was therefore mainly due to increased valuation multiples on the market in general as well as expectations of the benefits of a complete reorganisation based on a strategic plan. This strategic plan aimed at a high growth rate (particularly in large project activities), an increase in profitability through restructuring and the sale of some activities as in the UK as well as project management improvement. Since 2006 the group's financial performance has in fact improved. A number of sales were also made in 2007/8:

- FACEO, completed in Autumn 2007;
- Real estate assets in France, sales process started up in 2007, resulting in a transaction in Cegelec's favour in April 2008.

Through these changes Cegelec's net indebtedness was almost entirely reduced. By selling off Cegelec, LBO France aimed to capture the value created in the form of capital gains.

Description of ownership structure and how the transaction was realised

The outcome of the process of the sale of Cegelec was announced in January 2008. The selection process took almost six months. Serious bidders were:

- *Vinci and Eiffage*. This would have led to the consolidation of Cegelec in connection with a long-term industrial strategy. However, this solution would involve major risks in terms of employment and labour relations:
- *Pamplona* - an investment fund backed by Russian funds. A takeover by Pamplona could have opened the door to the markets of Eastern Europe and the former Soviet Union.
- *QD*

Financial market turmoil limited the capacity of funds to raise the debt that would be required to take over Cegelec. This is illustrated by the fact that Axa Partners - the first PE fund to approach Cegelec - did not end up submitting an offer.

In June QD's bid was confirmed. This project was submitted to the Information and Consultation Process of the European Workers Council and to other legally required industrial relations procedures according to laws in the countries concerned. The deal was completed in October.

There were two subjects of concern at the time. The first was the question of how the debt would be financed. The second was the administrative procedure by the French Ministry of the Economy and Finance regarding Cegelec's activities in strategic sectors in France (see below). Cegelec was the first operation of this size in France involving a SWF.

The valuation of Cegelec between the beginning of 2006 and mid-2008 increased by over 50%, from € 1.1 billion to € 1.7 billion. There are objective factors which explain this increase, above all the improvement of and prospects for the Group's financial results. Beyond these factors, a deal is always "clinched" based on a price which must be negotiated. The price will be what the buyer is willing to invest and what the seller is willing to accept, depending on their own resources, objectives and strategies and other factors. It was known that QD had considerable resources.

Capital gains correspond to the difference between the price paid for the Cegelec shares (+ € 1.200 million) and the value of the equity contributed by LBO France at the time the transaction is implemented (+ € 300 million), i.e. an increase of € 900 million.

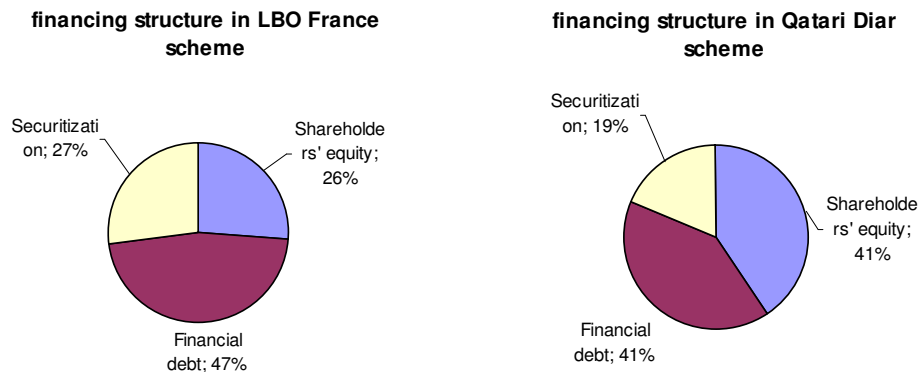
LBO France was the first beneficiary of these gains, as it held around 86 % of the capital of Cegelec. Management held 11% and employees 3%. The demand of trade unions for an exceptional prime distribution for employees was rejected; LBO France believed that the employees' share participation was the normal way to benefit from these gains.

A holding company has been set up to take over Cegelec Holding, which held Cegelec SAS. This holding company is owned by QD and took over control of Cegelec in October 2008.

The financing of this operation was based on € 700 million of shareholders' equity (60% in convertible bonds) and €1 billion in financial debt, including securitization debt (> € 300 million).

This operation has introduced two main changes for Cegelec. First, the planned scheme is not a classical LBO, as was the case with LBO France or other Private Equity funds. The amount of the equity would be higher, representing 40% of the financing. Qatari Diar's contribution is in line with its outspoken strategy of committing itself over the medium or long term. Qatari Diar's initial financial return would most likely be generated mainly through interest paid on convertible bonds.

Comparison of Cegelec Financing Structures



Source: Wilke, Maack and Partner

Although the level of debt would remain high, thus allowing leverage effect, the debt would nevertheless be lower than in the previous scheme. In addition, if the State of Qatar guarantees the debt, the carrying cost of this debt would be lower. From this standpoint, the debt will be even easier to bear by Cegelec if the business plan is successfully implemented and financial returns improve. This financing structure appears to be consistent with a long-term shareholder strategy.

Second, QD has stated its intention to make Cegelec a showcase of best practices in labour relations. Making the company more attractive to work for is a priority for QD. The commitment of employees to the company's projects and profit sharing in these projects are stated objectives for QD. Opening up the capital to employee investment is a first step. The scheme being contemplated would allocate a portion of the capital to employees which would be twice as high as for the transaction set up by LBO France in 2006 and would include employer contributions and incentives.

Strategy of the financial investor

QD believes that purchasing Cegelec will allow it to acquire or 'in house' skills which will be useful in connection with its development strategy. In the summer of 2008 QD was involved in over 40 real estate projects throughout the world representing a volume of approximately \$ 40 billion of which 40% were in the Middle East, 30% in Africa, and 30% in Europe (some projects have been launched whereas others are in the study phase):

- With Cegelec, QD acquired technologies and skills which are useful to design and perform these projects, in particular in the heating, ventilating, air conditioning, transport and energy fields, among others.
- QD has stated that it is interested in Cegelec's information system, its business tracking methodology, and its training policy. Moreover, its stated intention is to transfer these to the entire QD structure and engage in the transfer of know how.
- QD believes that its own business should provide Cegelec with a catalyst for growth. The Fund believes that Cegelec - considering its current resources - could develop at

the rate of one country per year. The initial objective is to position Cegelec within various projects underway in Qatar, such as the Lusail project with Qatar Petroleum. In addition to the business generated by the projects, QD is already involved in these geographical locations. This could lead to an expansion by way of follow-on business.

- This capacity to generate growth is important to QD, as the fund believes that growth now constitutes the best leverage to improve the Group's financial results, even if there is room for improvement in the area of profitability.

In addition, the acquisition of Cegelec would provide QD and the Qatar SF with recurring sources of revenue, in particular via Cegelec's European businesses (CFB, CBB, CGB, GSS, etc.).

It is important to point out that this is the first acquisition of this size and type by QD. Governance is a major issue for QD, which as most sovereign funds used to leave great autonomy to its portfolio companies. In practice, governance will involve a supervisory board representing the shareholders and a management board representing the general management of the company. An important change will be the departure of the long-standing CEO, Mr. Darmon, who is now more than 65 years old.

11.5 Consequences for core business

The takeover by QD has resulted in a change in corporate governance because Cegelec works in three strategic sectors in France: defence, aerospace, and the nuclear industry. For business in the defence industry, direct foreign investments are subject to an administrative procedure handled by the French Ministry of the Economy and Finance. Some business must be approved by a specific governance procedure involving State representatives.

Since 2008, Cegelec has not benefitted from QD projects, despite the fact that this company is involved in many investments in which Cegelec could be involved. This is a challenge for the next year.

With the deteriorating financial environment since the crisis the negotiation of debt has become more difficult. The economic recession and the worsening of the economic perspectives of Cegelec have made this investment less profitable. Some resulting changes in the company's organisation cannot be ruled out.

11.6 Economic development of the company and employment

The analysis of the economic development of Cegelec involves some difficulties. There is very little public information on Cegelec finances, since a private company has few obligations in this respect. However from various sources, it is possible to put together some relevant points which we outline below.

First, the period from 2001 to 2005 was a period of consolidation for Cegelec. The company had been formed in 2001 by Alstom Group, on the basis of Alstom Contracting. It included some activities which were not part of the core business and some subsidiaries which were facing difficult market conditions e.g. in northeast France and in Germany. In order to deal with this situation Cegelec followed a dual strategy: cost reduction and cash generation. This led to the sale of some subsidiaries in the UK and Luxembourg; financial and working capital changes; a slowdown in acquisitions due to financial restrictions; lowering of general expenses; a search for increased flexibility through subcontracting and temporary employment; and employment cost reductions. These resulted in almost 2,000 fewer jobs in Europe (or a reduction of 10%). All areas were affected, especially blue collar employment in Northeast France and Germany. This involved more than € 60 million in restructuring charges. Over this period revenues were quite stable (around € 2.8 billion) and EBIT under € 100 million.

Second, the secondary LBO was done with the aim of development and profit growth. In fact Cegelec has met its objective with growth (+7.5% in 2007 to € 3 billion). EBIT increased a strong 29% to € 48 million through cost cutting, project management improvement and accelerated cash generation.

Third, regarding the present period, orders received in 2008 should allow Cegelec to resist the crisis in 2009. The impact of the crisis on Cegelec will be clearer in 2010 and 2011. As was mentioned above until now QD has contributed very little to Cegelec's business development. QD's strategy thus could be a key issue in dealing with the crisis.

11.7 Comparison of company development with branch average

The competition for large project activities is international. But the bulk of Cegelec's activity is local. This involves local competitors, some of which have attained a significant size and are involved in a number of European countries. Among them there are:

- Vinci Energies and Forclum which are backed by large civil engineering firms (Vinci and Eiffage). Bouygues also has a specialized subsidiary ETDE that is somewhat smaller than the other firms. Vinci Energies is the leader in the French market.
- Suez and its subsidiary SES (Energy Services) that includes Ineo and Fabricom. Suez is the leader in Benelux and Imtech in the Netherlands.
- Spie, which is independent, belonging to PAI Partners through an LBO in 2006.

Until 2005/2006 Cegelec compared with its main competitors in terms of growth was underperforming and was losing market shares in France. No acquisitions were made due to financial constraints. But during that time Cegelec greatly improved its financial discipline and became one of the best companies in working capital management.

Since 2006 Cegelec has made several acquisitions. Its growth trend has been much more in line with its main competitors. This happened in a context of economic growth in France and a positive development in the sector, as the following figures show.

France – main economic indicators

	2003	2004	2005	2006	2007	2008
Real GDP growth rate	1.1	2.5	1.9	2.2	2.3	0.4
Employment rate in %	64.0	63.7	63.9	63.8	63.6	65.2
Unemployment rate in %	9.0	9.3	9.2	9.2	8.3	7.8

Source: Eurostat

France- Manufacture of machinery and equipment

	2002	2003	2004	2005	2006
Enterprises	8,730	9,202	9,201	9,204	9,157
Turnover in € mio.	25,168	25,353	27,062	28,079	30,623
Employees	148,174	145,539	143,711	141,365	138,396

Source: Eurostat

11.8 Consequences for employment and industrial relations

It is too early to fully appreciate the consequences of the takeover of Cegelec by QD for employment and industrial relations. However, one major difference with respect to previous years is that there is less financial pressure on Cegelec, as it is no longer permanently 'up for sale' with a large debt to cover. Previously the future of Cegelec and thereby of employment and the pressure on costs were the main subject of industrial relations.

The fact that the QD investment can be considered as a medium- or long-term investment is likely to have an impact on industrial relations. Even if the crisis has changed the perspectives of Cegelec and QD, some issues may be singled out in terms of industrial relations:

First, QD has taken over the Business Growth Plan and retained the management of Cegelec. QD's acquisition could improve the capacity and organizational ability to work at the international level and in new countries outside of the Group's historic playing field. Moreover, the ambitious growth strategy of QD could lead to consolidation with other industrial groups.

Second, representatives from QD have stressed their appreciation of the skills which Cegelec's employees possess. These skills are greatly needed to develop QD's business. They have not identified any negative synergies in terms of jobs with other companies they already own or with the joint ventures set up with Suez and Vinci. On the contrary, QD has stated that the Group's headcount should increase at all levels of qualification.

However, QD believes that, from a labour relations standpoint, Cegelec is not among the 'best in class' in the industry, compared e.g. to Vinci and other major competitors. The Fund has stated its intention to make Cegelec a showcase of best practices in labour relations. QD has stressed several times that the Group is having difficulties attracting and keeping new talent, in spite of the positive image of the Cegelec University and its training reputation. A representative from QD has spoken to the EWC on this matter and on the strategy of QD.

Third, making the company more attractive to work for constitutes a priority for QD. As regards this point, the commitment of employees to the company's projects and profit sharing in these projects are stated objectives.

QD has announced that it will deal with these issues in two ways: by opening up the capital to employee investment and by introducing employee profit sharing based on company performance. Although the legal and tax frameworks applicable to bonus and profit sharing systems are different depending on the country, the intention is to introduce a general system throughout the company.

Fourth, the intention of QD to make Cegelec a 'showcase' for best practices in labour relations is naturally part of its growth and acquisition strategy. The impact of the take-over of Cegelec by QD is limited in terms of employment, thus it remains the case that labour policy constitutes a major challenge for the Group.

With this in mind, the members of the European Works Council have been engaged in a strategy regarding sustainable development and have identified five priorities: employment; corporate strategy and its impact on employment; improvement of working conditions and remuneration, including training; health and safety; and subcontracting. This strategy is not in contradiction with the stated intentions of QD. It has to be linked with the strategy of Cegelec and QD in sustainable development, new facilities and "green" projects.

11.9 Summary and lessons to be learned from this case study

From 2001 to 2008 Cegelec was driven by an LBO logic oriented to the short term sale of Cegelec and a high return on investment for the fund, based on the growth of valuation of Cegelec and its debt reduction. The first LBO (2001-2006) helped restructure Cegelec's business and financial situation,.However this had a high social cost. The second LBO (2006-2008) was based on growth. Two good asset sales accelerated the process and helped lead to the sale of Cegelec.

Even if PE funds were candidates for taking over Cegelec, the LBO model was reaching its limits. The higher profitability aimed at by PE funds was based on continual growth, permanent profit improvement and low interest rates. These changes and higher valuations on the financial markets led to an increase in the company's value. The capture by the funds of the resources generated by the firm did limit its capacity to develop in the medium- and long-term. The permanent availability of the company for sale also did not help to build a long term strategy. Therefore, the Private Equity Fund strategy and financial constraints (i.e. covenants and interest payments) limited Cegelec's ability to invest and to grow as fast as its major competitors (especially after the first LBO).

From this point of view the arrival of QD can change the situation for Cegelec. In particular this can give more stability to the firm. Moreover, profitability now is analysed on medium and long term (and not on the gain generated by a short term sale). Therefore there are three challenges for Cegelec. The first is to build a new governance system, since QD used to be not represented on the boards of directors of the companies. This acquisition reveals a strategy change for QD, e.g. investing in the capital of Suez Environment. The second is to develop a new framework for industrial relations. On the one hand trade unions and workplace representatives are expecting changes. On the other hand, the quality of industrial relations belongs to the development strategy of QD. Qatari Diar's intention to make Cegelec a "showcase" for best practices in labour relations may support a strategy of acquisition. The third challenge is to build synergies between the businesses of Cegelec and other partners and projects in which QD is involved.

12 P&O/United Kingdom: A case study of a SWF investment

12.1 Information – PE, HF and SWF Investments

The UK is by far the most significant of the six countries in this study for private equity and hedge funds (in both cases as both a headquarters for fund management and a location for investment) and for sovereign wealth funds for an investment location. Private equity investments in domestic firms peaked in 2006 at 1.26% of GDP. Since UK-based PE funds invest heavily in other countries, investment by UK-based PE funds was even higher in that year (2.2% of GDP). Fundraising also peaked in 2006 at € 75 billion. Buyout investments clearly dominate, accounting for between two thirds and four fifths of total PE investment.

The UK (in particular London) is the second largest international center for HF management (after New York) and accounts for approximately four fifths of European HF assets under management (estimated at \$ 270 billion at the end of 2008 by International Financial Services London). The largest HF positions in companies listed on UK stock exchanges appear to be relatively modest compared to this total figure, in part due to lack of transparency, in part since HF massively sold their long equity positions in the second half of 2008 and built up large short positions. With one exception, the largest 20 identified HF positions at the end of 2008 accounted for less than 2% of shares outstanding of UK-listed companies.

SWF positions in UK-listed companies were considerably larger and more concentrated. Positions at the end of 2008 were as large as \$ 4.4 billion (Temasek Holdings position in Standard Chartered) and 27% of shares outstanding (Qatar Investment Authority's position in Sainsbury's).

Here it must be stated in the UK context that the model takes various forms. These range from the acquisition of a relatively small number of shares for a relatively short-term, to the acquisition of a larger proportion of shares on a longer term basis, through

to the acquisition of a whole company. The case of P&O and DPW is at the latter end of the spectrum, though later it also engaged in a flotation and a restricted share offering. Thus, in the case of DPW, we have an example of an acquisition, taking the company private, and then a subsequent floating on a new stock exchange, but with restrictions on the sale of shares.

The activity of SWFs in the UK is, along with Germany and France, towards the higher end of the SWF spectrum in terms of size and coverage. This may lag behind SWF involvement in the US, especially recently in financial companies in that country. In the UK and Europe, involvement has been across a wide spread of sectors, including manufacturing and services of various kinds.

The consequences of acquisition by SWFs for restructuring, employment, jobs, and industrial relations have to date been less than the activity of PE funds. However, as will be shown below, this is not insignificant in the case of DPW and P&O.

12.2 P&O – SWF as strategic investor

Introduction: why the case was selected

The case of P&O and DPW was chosen for the following reasons. First, P&O has long been one of Europe's largest shipping and ports companies; it had already gone through a period of substantial restructuring prior to being acquired by DPW. Second, DPW is predominantly owned by Dubai World and in turn by the government of Dubai and was already itself one of the world's largest ports operators. The acquisition gave it a stronger position in Europe and elsewhere in the rest of the world. Third, as will be explained below, DPW is an interesting variant on the SWF model. Fourth, both the process of acquisition and the consequences of the acquisition provide interesting examples in any study of fund activity.

Interviews were obtained with all the trade unions involved in the sector in the UK Rail Maritime and Transport (RMT), Transport & General Workers Union (TGWU), and Nautical (the officers' union) and also with the International Transport Workers' Federation (ITF) which coordinates international organisation in the sector. These provided useful information and insights. Unfortunately, despite numerous approaches, P&O / DPW was not prepared to be interviewed and, as a result, from the side of the company and its acquirer, reliance has had to be placed on secondary data in company reports and in the press.

12.3 Profile of the company and the financial investor⁵⁹

The company P&O (Peninsular and oriental steam navigation company)

P&O was one of the UK's oldest established companies. Founded in 1837, it played a significant role in shipping between England on the one hand and Spain and Portugal on the other. Rapidly it extended its shipping operations throughout what was then the British Empire and beyond. In the interwar years, it owned a fleet of almost 500 ships. Over time, it moved into port operations and later ferries. Along with the German company, Hapag, it was Europe's largest company operating in this sector.

Core businesses, strategy, and reorganisation

In the 1980s and early 1990s, P&O had a number of businesses – cargo shipping, cruise ships, ports operations, ferry companies, real estate, and construction. In the 1970s, it

⁵⁹ The case study is based on public available material. Additionally interviews have been made with representatives of the International Transport Workers Federation, the Transport and General Workers Union, and the Rail Maritime and Transport Workers.

had diversified from its maritime base into oil exploration, exhibition centres, property, and construction. In effect, at that time, P&O was something of a conglomerate, with the advantages (scope and hedging) and disadvantages (lack of focus and looseness) which conglomerate status entailed.

Performance of DPW and main competitors, at selected dates, ports terminals, and related only

	2006				2007				2008 provisional periods			
	APMM	HW	SPA	DPW	APMM	HW	SPA	DPW	APMM	HW	SPA	DPW
EBITDA	20%	19%	63%	N/A	23%	24%	66%	20%	27%	26%	N/A	25%
Income Margin	14%	14%	40%	N/A	16%	17%	53%	45%	21%	15%	N/A	22%
ROE	28%	9%	28%	N/A	32%	12%	31%	16%	24%	6%	N/A	4%
ROCE	16%	5%	10%	N/A	19%	6%	14%	9%	14%	3%	N/A	3%
Current liquidity ratio	1.5	1.4	1.0	N/A	1.3	1.3	0.7	2.2	1.1	1.3	N/A	1.2
Cash flow/debt	0.2	0.1	0.2	N/A	0.4	0.2	0.2	0.2	0.2	0.1	N/A	0.1
Debt/equity	0.7	1.0	1.8	N/A	0.6	0.8	1.2	0.7	0.6	0.8	N/A	0.6
Staff cost / operating expenses	15%	17%	45%	N/A	14%	18%	48%	30%	N/A	19%	N/A	NA

APMM: A P Moeller-Maersk, HW: Hutchison Whampoa, SPA: Singapore Port Authority, DPW: Dubai Ports World.
Source: Company accounts and various

The ownership of P&O was like many large UK companies, namely there were no single large blockholders, shares were widely dispersed, and the company was actively traded on the London Stock Exchange. This had left management free to pursue various strategies, in particular related and unrelated diversification and then de-diversification. Under a number of strong and charismatic chief executives, these strategies were carried through, but with increasing pressure from shareholders, especially institutional shareholders.

In the late 1990s the company divested itself of its construction business and then later of some of its property assets. This was under pressure from investors in the City of London and was seen as a good thing by the financial markets. In 2000 it sold its P&O Princess Cruises to the American company Carnival. Later, in 2005, it sold its stake in its container shipping operations, Royal P&O, to the privately held Danish company, AP Moeller-Maersk, for £ 381 million. Increasingly there was also talk about the possibility of selling off ferries, not least because of growing competition from the Channel Tunnel and from low cost airlines. As a result of the trajectory of growth in businesses and these divestitures, the company had come increasingly to concentrate on the highly profitable port terminals and logistic business, which had grown steadily over the years and was growing rapidly in the 1990s and 2000s with the expansion of world trade, especially trade with Asia. However, it also continued to own a substantial ferry business (between the UK and France, Belgium, Netherlands, Spain, and Ireland)

Organisation

By 2006, therefore, on the eve of the acquisition by DPW, P&O had already substantially restructured and was organised into three businesses – ports and terminals, logistics, and ferries. One of the jewels in the crown was a set of port operations which P&O had throughout the world, but in particular in Asia, Europe, and North America. P&O was also likely to be chosen to be the developer and operator of the massive new Thames Gateway port in the UK. Altogether, this made P&O the fourth largest container port operator in the world. However, it should be noted that, in terms of ports, it was said to earn 90% of its operating profits from outside the UK.

By this time also, the company was less of a conglomerate and more of a focussed and centralised divisional type firm. It had also gone a long way to sort out and increasingly to centralise its managerial hierarchy. Local management in UK used to come from the ships and were internal promotions and each port had its own HR manager. But, after a fundamental business review in 2004, senior managers were increasingly brought in from outside and decision making came to be centralised in London and in Dover.

The financial investor DPW

It should be stated at the outset that the names and relationships of funds and companies in Dubai are closely interconnected. They are not always too clear to the outsider and, without assistance from DPW, it was difficult to put this aspect of the story together.

At the time of the acquisition, DPW was owned by the government of Dubai, via a holding company. In turn the holding company is under the control of the ruler of Dubai, HH Sheik Mohammed bin Rashid Al Maktoum, who was also the prime minister of the United Arab Emirates.

Dubai World is the above-mentioned holding company and government-owned conglomerate. Under its umbrella are the following: DPW; the investment company Istithmar, the property developer Nakheel; and a number of other funds and companies. As for DPW, though its operating origins go back into the 1990s, it was itself only created in 2005, according to some accounts. According to other accounts, DPW is itself a subsidiary of Ports & Free Zone World which is itself a subsidiary of DW. Put another way, DW covers four sectors – transport & logistics, ports and marine, urban development, and investment and financial services. DW is said to be one of the largest holding companies in the world.

Dubai in context

Dubai is one of the seven emirates which make up the federal UAE. It has a population of 1 million, of whom 75% are expatriates. It is not oil rich, but benefits from its membership of the UAE and is an important trade centre. Politically, the state is dominated by the royal family and a small elite; it is politically stable and pro-business.

The aim of Dubai from the 1980s / 1990s onwards has been to diversify away from dependence on oil. Using its own financial resources and extensive borrowings, it has promoted transport, financial, and tourism services. Most relevant to this case study, it has aimed to become a major transshipment centre and to develop and sell maritime and port expertise throughout the world.

In addition, to DW there is also the Investment Corporation of Dubai which is a further investment arm of the government of Dubai, with investments in Dubai, elsewhere in the Gulf, and elsewhere in the World. Port & Free Zone Worlds FZE is another entity, whose exact status it was not possible to clarify, but which is referred to as the owner of DPW. The top personnel of the organisations overlap considerably and often have the same chairmen.

It might be argued that DPW is not really partake of the SWF form, but is a free standing state enterprise, like many other enterprises in the world. However, it should be countered that it is obviously a part of DW which is the organisation under which a number of related funds and companies are to be found. According to the SWF Institute, the Dubai Investment Corporation with \$ 82 billion in assets is 12th largest SWF and DW the 52nd in the world. The former is given a middling transparency rating and the latter no rating by the SWF Institute. In many respects, DPW is rather like Qatari Diar and in this respect they constitute good comparisons, though they operate in different sectors and in different ways.

In terms of organisation, it might therefore be said that DPW has a corporate entity, with some outside shareholding which will be referred to below. But it operates under a holding company which has a number of companies and funds under its umbrella and has been able to draw on extensive financial resources within Dubai and the UAE.

In DPW, top decisions would seem to be made by senior managers from Dubai. However, in operational terms, DPW is relatively 'hands-off'. As one union interviewee commented, 'You don't see them or hear them... it's often as though they are not there'

Operations, strategy, and aspirations of DPW

The port complex in Dubai constitutes the world's tenth largest port and has benefitted greatly from the long boom in world trade, especially between Asia and Europe. The home operations of DPW are at Jebel Ali and Port Rashid and were built up, steadily and then rapidly. This signifies the desire by the Dubai government to diversify its commercial activities.

Thus, at the time of the P&O acquisition, DPW was the seventh largest port operator in the world, having already in 2005 acquired the international terminals of the US group CSX Corporation which itself had been a large global operator.

Those in the government and related business and investment funds have had the aim of making DPW into one of the top three or four ports operators in the world. Dubai is seen as in an excellent geographical position to attract world trade. The home operations had been built up with this in mind. In addition, port operations have been developed in other countries in the Middle East, Asia, and Europe. The possibility of acquiring P&O offered an important strategic opportunity to develop further in Europe and Asia.

12.4 The acquisition process

In the early 2000s, commentators felt that P&O had considerably restructured and was a very successful company. There was no talk of it actively looking for acquisitions or for itself to be the subject of a merger or takeover. However, some saw the disposal of various assets and a fundamental review of business operations as a 'clean-up' operation before the company itself could be sold off.

When bidding started for P&O in 2005, it soon became a competitive bidding process. Potential bidders included Denmark's A P Moeller-Maersk, Hong Kong's Hutchison Whampoa, and Singapore's SWF Temasek. It should be noted that none of these were publicly listed. In the end, the bidding came down to the Dubai and Singapore authorities: a bid was first agreed from the former for 443 pence per share; this was followed by an agreed bid of 470 per share from the latter; but in turn this was trumped by a bid of 520 per share from Dubai. This was said to be at a 70% premium on the share price, reflecting how much these two state entities could afford to bid. The agreed price valued the company at a very high figure of around for £ 4 billion. As such, the takeover was the one of the largest ever transactions in the Middle East.

The acquisition was an all-cash operation. To finance this, Dubai had arranged facilities totalling \$ 6.5 billion, incorporating a \$ 6.3 billion term loan facility and a \$ 200 million revolving credit facility. Simultaneously, these credit facilities were also to be used to refinance existing debts.

Investors, including hedge funds, were said to have read the bidding war well and benefitted considerably from the sale. In addition, existing and past top management were said to have made large sums from the deal through exercising options and incentive shares.

There is an interesting side story to the bid which involved a ruckus in the US. P&O operated a number of major ports and some minor ports on the eastern seaboard of the US. This had always been thought to be unproblematic. However, it was argued that sale to an Arab investor would be a threat to national security. Despite this, the Bush administration approved the sale, but Congress objected. This led to the involvement of the Committee on Foreign Investment in the United States (CFIUS), a panel which judges on foreign acquisitions which might raise security or anti-trust questions. In the

end, the US ports were taken out of the deal and sold separately to American International Group (AIG) asset management division, for an undisclosed sum.

The strategy of the financial investor DPW

The strategy of DPW is to develop containerised cargo handling based on long-term contracts to operate terminals in ports throughout the world, with a particular focus on Asia, the Middle East, and Europe. This would seem to be a long term strategy, based on acquiring both port facilities and the operational know-how to operate them and also selling wider services to others in the maritime business. More fundamentally, on the part of Dubai and its rulers, this is part of a long-term strategy to develop national capabilities in what are seen as growth industries, such as financial, transport, and tourism services.

At the time of acquisition, the company stated: 'DPW is owned by a single shareholder, the government of Dubai. We are run entirely on commercial terms, and, with private ownership, we are able to take a long-term strategic view and make substantial investments'. Again, it was stated, 'This is not a portfolio, it is a strategic investment.

Once acquired, P&O was delisted from the London, Sydney, and Tokyo exchanges where it has previously been listed. P&O headquarters were left in London, but it is clear that increasingly key decisions are made in Dubai.

In October 2007, Sultan Ahmed Bin Sulayem, chairman of DPW, announced that 20% of DPW would be floated on the Dubai International Financial Exchange (DIFX), now called Dubai Nasdaq. The IPO was to be in the form of a sale of shares by DPW. Subscription eligibility was restricted to residents of the UAE and nationals of states belonging to the Gulf Cooperation Council. There is also in the press reports reference to eligibility globally of institutional investors, but it was not possible to investigate the significance of this. To-date, the IPO was the largest in the history of the exchange and the biggest flotation ever seen in the Middle East. Port & Free Zone Worlds FZE is reported as owning 80.45% of the shares in the 2008 Annual Report.

12.5 Consequences for the core business

P&O now appears on the DPW website as a services company, providing port, cargo, chartering, and agency services of various kinds to a spread of customers. To date, there have been no significant divestments by DPW of P&O assets.

There was some speculation that DPW did not really want the UK ferry businesses which were deemed by some not to fit with its core business. It was speculated that this business might be sold off. However, this has not happened. This may be in part because some parts of the ferry business have been good income earners, in particular Dover cross-channel ferries. Moreover, at the present time, P&O is in the process of having two new 49,000 gt ferries built which will enter service in 2010 and 2011. This is seen in the industry as presaging a long-term commitment to this part of the business. However, there is now renewed speculation that at least some parts of the ferries, namely those sailing out of Hull and Portsmouth, may be sold off or closed down. This is said to be a consequence of the poor returns on these particular routes. It is also said that this would have been considered anyway by whoever owned the company.

12.6 Economic development of the company

It is difficult to give a multi-year assessment, because DPW did not exist so far back and data is not available. Table 1 gives a first impression of the position of P&O compared with other major companies in this sector.

In terms of investment policy, to date, investment has been forthcoming in the ports and terminals operations which is a highly capital intensive business. As stated above,

there is also investment in the ferries business. The source of funds is not always clear to the outsider. However, there would seem to be transfers within DW and use of retained earnings. Of course, the flotation in 2007 also raised funds. In addition, DPW has a \$ 5 billion bond and a further \$ 0.8 billion sukuk (Islamic) bond.

In terms of market performance, see Table 1 below. Given the short period since the acquisition, it is difficult to say what effect this has had on performance. In addition, of course, the advent of the world economic crisis from 2008 onwards has also affected markets and performance. All in all, both P&O and DPW had been on a significant growth trajectory in the ports and terminals business, but this has now slowed down or come to a halt.

12.7 Labour relations and the development of employment

The P&O inheritance

Up until the 1980s, P&O had pursued policies which largely fitted with those of most British companies. In the UK, where there were trade unions, these were recognised. P&O had been a member of employers' organisations in the sectors in which it operated, but had gradually left these and come to conduct its industrial relations internally within the company. Terms and conditions were at least on a par with those of other companies in the sectors in which it operated.

From the 1970s and into the 1980s, in the UK, P&O was involved in dramatic changes in the docks in the form of containerisation and moves to new port facilities away from older ports in London, Liverpool, and Southampton. At the industry level, this involved some confrontations with labour and a weakening of the power of unions. In 1989 the Dock Labour Scheme which gave security of employment to dockers was abolished.

More specifically, in 1989 a complex set of factors had led to P&O taking on the trade unions which organised ferry workers at the port of Dover. The issue was terms and conditions. This was a major dispute which lasted for one year. It involved the use of replacement labour and major confrontations between the company and strikers. As such, it was one of the major industrial disputes during the Thatcher government years. Ultimately the dispute was settled in favour of management. The unions were de-recognised at Dover, alternative company-based representation arrangements were established, and pay and conditions were unilaterally changed.

However, it should be noted that P&O did not seek to derecognise unions in other ports or in other operations nor did it derecognise the officers union at Dover. Recognition for seaman was only restored at Dover after the election of a Labour government in 1997.

Further in the early 2000s, the company continued to tighten up its operations and on working conditions. They also transferred employment contracts off-shore, and increasingly UK labour was replaced by Spanish seafarers, then Portuguese labour, and more recently workers from Eastern Europe, the Philippines, and the Indian sub-continent. By some, this 'sorting out' was seen as a prelude to the sale of the ferries and perhaps the whole of the company.

In 2004 the company carried out a 'Fundamental Business Review' which, for the ferries, involved redundancies, changes in working methods, and some standardisation on Dover. The union was consulted on these matters.

In Europe and the rest of the world, P&O's policy was to leave labour relations to local management which dealt with them according to domestic practices. This involved some major disputes with unions, in particular at various times in Argentina and Australia.

The development of human resource and employment practices after the acquisition

It proved difficult to obtain hard figures on employment for P&O in particular and DPW in general. At the time of the acquisition, P&O was said to have 22,000 employees worldwide. However, this may have been much higher, given the use of subcontract and temporary labour in large parts of the ports business. In 2008 DPW refers to 30,000 employees. This would seem a reasonable estimate, given the prior size of DPW, its acquisition of CSX, and its acquisition of P&O.

To date, there do not seem to have been any significant reductions in employment. However, the financial press reports that the world economic crisis and the downturn in trade has started to affect the company. Restructuring is said to have begun, aimed at consolidating operations. In particular, there is growing fear among the unions that some ferry operations could be run down.

In terms of policy on employment and labour matters, the company states, 'While we adhere to local labour regulations and statutes, we emphasise that we are one company seeking common goals by having a common and consistent reward framework wherever possible' However, in practice, the company runs its employment policies through regions, with minimal central guidance.

12.8 Consequences for industrial relations

Human resource management and employment planning

Given the lack of cooperation from the company, it has proved impossible to ascertain whether there is a formal or informal employment strategy or plan which covers P&O and DPW, that is, beyond devolving many aspects of these areas down to regional and local level management.

However, there is no collective agreement or social plan which covers P&O in the UK, Europe, or world-wide. Even more so, there is certainly no such agreement or plan which covers DPW.

Recently DPW has made some announcements about its plans in the context of the world recession. These include a general review of operations and more specifically a freeze on recruitment and some labour related costs such as travel. At Southampton terminal in the UK, parts of the contractor labour force have been laid off and working hours have been reduced. There are also reports that further redundancies are forthcoming. In the UK, there have also been some job losses on the ferries, but not a large number.

Of its main competitors, Hutchison Whampoa seem to have gone further down the road of lay-offs, early retirements, cuts in pay, and changes in working, at least in its UK operations. Thus, DPW is not a leader in the sector in this respect.

Trade union recognition and representation

In the UK, trade union recognition extends to the following main unions – RMT for seafarers, TGWU for port workers, and Nautilus for professional staff such as ship's officers. Union membership is estimated to be very high for ship's officers (over 75%) and reasonably high for others in the UK.

Elsewhere in Europe, such as in the Netherlands, union recognition is in line with national laws and practice. No estimates are available on the level of union membership.

There exists for P&O a European Works Council. Some of the union representatives interviewed felt that the works councils was being increasingly used by management as a way of by-passing the unions. It was said to receive more information than the unions,

but basically it only meets about three times a year. However, all the employee representatives on the Council are union members.

Elsewhere in the world, unions would seem to be recognised in Australia. DPW does not recognise trade unions in Dubai. Overall, the company prefers to deal on a country by country basis. However, some union websites describe it as 'anti-union'

On a world-wide basis, the unions have difficulty entering into dialogue with DPW. They know that the managers talk to each other and manage labour on certain baselines. But, the unions have not been able to obtain a global framework agreement with DPW. At the same time, it must be added that the unions have much the same problem with the other big operators, though DPW has been the most difficult with which to enter into dialogue. AP Moeller-Maersk comes the closest to this.

Topics of negotiation and consultation

The union, works council, and workforce were informed after the decision to sell had been made, but they were not consulted as such. In addition, the unions have been informed that there is no intention to sell off ferries. Information has also been provided on pensions – for which, see below.

Pay and conditions are determined locally, either unilaterally by management or by negotiation and consultation depending on national circumstances. However, the unions feel that, within the UK, there is management 'behind-the-scenes' coordination in fixing pay and conditions. Across Europe there may also be some coordination of pay and conditions, by management, but again no involvement of unions in European wide consultation and bargaining.

In the case of pensions, there are some interesting aspects of the P&O case, but, given lack of cooperation from the company, it was not possible to investigate these fully. Initially, at the time of the acquisition, press statements pointed to the £ 200 million deficit in the P&O pension fund. It was also claimed that pension trustees had threatened to try to block the deal. As part of the bidding process, therefore, DPW agreed to put £ 125 million into the P&O pension scheme, with a promise of more to come over the following five years to clear the deficit. However, some union observers felt that this would have been reflected in the price which DPW paid for the company.

P&O had a number of pension schemes throughout the world. The principal scheme (referred to in the paragraph above) was located in the UK and is known as the P&O UK Scheme which covered ratings and officers. This was a funded defined benefit scheme and was closed to new members in 2002. It is the scheme into which DPW is paying the sums referred to above. A second significant scheme in which P&O participated was the Merchant Navy Ratings Pension Fund which is multi-employer defined benefit scheme. This was also closed to new members in 2002. It also has a significant funding deficit. The unions said that there is now a question mark over DPW's payment into this scheme; as a result, other companies complain that they have to carry a greater burden. Legal action is mentioned. A third scheme is the Merchant Navy Officers Pension Fund, also a multi-employer defined benefit scheme. This is now also closed to new members. Payments into this scheme have also been the subject of dispute between employers and some legal action.

The climate of industrial relations and social peace

There have been no disputes of any significance since DPW acquired P&O. There were also no major complaints from the trade unions about relations with the company, with the possible exception of the issues cited above. These include some fears about the ferries, some worries about the pension arrangements, and a felt preference by the company for dealing with the European Works Council as opposed to the trade unions

One union representative summed up the situation by saying that DP has not been 'heavy handed, or at least not to date'

Consequences for work organisation

At the macro level, as has already been stated, to-date, there have been no significant changes in the major parts of P&O which have led to major reorganisations, restructuring, or reductions in manning levels. Yet, also at the macro level, there is the concern as already cited about what might happen with the ferries. At the micro level, there is also no evidence to date of any major changes in working practices, involving the structure of jobs or the intensity of work. It might, however, be added that P&O had already engaged in such activity. Also, it may well be that it is still early days.

The DPW website makes considerable play of its investment in training and development. It states that DPW 'are committed to creating a safe and secure workplace and investing heavily in training and development at all levels so that employees can learn new skills and develop their careers within the organisation'. The unions confirmed that DPW met all statutory requirements on training of seafarers and officers. The P&O website also states that the company is a 'preferred employer', committed to training and development and equal opportunities.

12.9 The present economic situation and possible exit strategies of the Dubai investment interests and DPW.

At the present time, there is some admission by Dubai that the country may well have overextended and overleveraged itself in the period up to 2008. It is reported that Dubai has recently borrowed from the federal government of the UAE – in effect from its richer neighbour in Abu Dhabi – to help refinance its debts and assist government-affiliated companies to pay their bills. Dubai is also quoted in the press as beginning to restructure its sprawling government-affiliated conglomerates. In this connection, the 2008 Annual Report says that they have deferred half of their planned capacity expansion plans.

For the ports and terminal industry, over a quarter of a century from 1980, compound annual growth rates have been around 10% for, with much of the increase coming from Asia. Growth rate projections have now been considerably reduced. As with its main competitors, DPW is now looking to cost reductions. In addition, they have announced the cancellation or delay of capital expenditure of various types.

In terms of exit strategies, DPW is not a case, such as a HF, PE, or many SWF situations, where the intention is to exit at some point in the future, via a sale of shares or a public offering. As stated above, DPW has already floated part of the company to some other investors on the Dubai stock exchange. DPW would seem to be in the business of ports operations for the long-term as part of a national and corporate development strategy. However, this does not mean that it will not divest itself of some of its activities, which might include part of ferries.

12.10 Comparison of company development with branch average

There are now four main players which control about half of world container trade, A P Moeller-Maersk, Hutchison Whampoa, Singapore Port Authority, and DPW. It is difficult to say which is largest - A P Moeller-Maersk or Hutchison Whampoa - and this differs anyway according to the measure chosen. In effect all four companies have all become truly global players in the 2000s, since before that they were largely regional players. (see Table 1 for comparable figures).

A P Moeller-Maersk (a family controlled business) has activities in 4 sectors – containers and terminals, shipping and offshore, retail, and energy. The first activity contributes a rising proportion of revenue. The company suffers from some problems with its other

activities, but in the ports area has high returns and good liquidity. Its debt is said to be well-structured bank finance. It is also said to have relatively low staff costs and a flexible cost structure in the ports area.

Hutchison Whampoa is more of a conglomerate and has five core businesses – ports and related services, property and hotels, retail, telecoms, and utilities. It is also a family business, though Temasek / Singapore Port Authority owns a minority stake. The company has grown significantly and is adjudged to have a flexible cost structure and good liquidity. Staff costs are relatively low.

The Port of Singapore Authority is controlled by the Temasek SWF. It has also grown significantly and has good returns, but it is said to have a relatively inflexible labour cost structure. DPW is now the third or fourth largest terminal operator in the world, depending on which measures are used. It is also one of the most geographically diversified, with 49 container terminals, in 31 countries. It has relatively lower margins and higher debt obligations than its competitors. Its staff costs are said to account for 30% of total operating expenditure – also relatively high compared with competitors.

In terms of employment relations, A P Moeller-Maersk has made no announcements of cost cutting plans affecting employment. It is good at dialogue with the unions in Europe and would be expected to consult and inform unions, again at least in Europe.

Hutchison Whampoa has made no global announcements about employment matters since the crisis. Staff costs are said to be relatively low. However, there are job cuts and reductions in pay and conditions at Felixstowe in the UK. The company is said to be friendly to labour in Europe, but can be tough elsewhere.

PSA has made no declarations on employment or job cuts, but it has made significant redundancies in the past and industry observers do not rule this out in the future.

In fact, DPW is the only company which has made announcements about its employment plans. These include a general review and more specifically a freeze on recruitment and some labour related costs such as travel. At Southampton terminal in the UK, it has laid off parts of its contractor labour force and reduced working hours. They have announced that further redundancies are forthcoming. Such reductions in employment will be made in consultation with unions and employees in the way described in sections above.

The whole process took place in a very friendly macro-economic environment with annual growth rates near 3%. The branch situation in transport and storage was also characterized by a growing turnover. However, employment slightly decreased from 2005 on.

United Kingdom – economic indicators

	2003	2004	2005	2006	2007	2008
Real GDP growth rate	2.8	2.8	2.1	2.8	3.0	0.7
Employment rate in %	71.5	71.7	71.7	71.6	71.5	71.5
Unemployment rate in %	5.0	4.7	4.8	5.4	5.3	5.6

Source: Eurostat

UK – Transport, storage and communication

	2002	2003	2004	2005	2006
Enterprises	82,012	82,233	79,119	81,793	81,762
Turnover in € mio.	295,833	274,169	293,276	311,564	322,520
Employees	1,620,012	1,600,461	1,601,726	1,634,497	1,560,500

Source: Eurostat

Other known investments of the financial investor in the same branch

According to the SWF Institute, DW has the following major direct foreign investments: (public) Labroy Marine Singapore (98.4%) and MGM Mirage US (8.87%); private ESPA

International UK (40%) and Beng Kuan Marine China (37.88%). The investment fund which comes under the DW umbrella, Istithmar, is listed with a number of other public and private investments, ranging from maritime, to industrials, retail, and services. DPW has a number of subsidiaries in the Europe, Asia, and Australia, as listed in the company accounts. The SWF Institute gives a separate listing for the Investment Corporation of Dubai which it also describes as a SWF, with several operating investment companies. It is listed with a number of other major direct foreign investments, both public and private, in the US, Europe, and Asia. These cover financial services, hotels, autos, and engineering.

12.11 Summary: lessons to be learned from this case study

P&O was a major UK, European, and world company in its sector – shipping, ports, and related logistics. It had considerably restructured itself in the twenty years before acquisition by DPW. This made it both a strong independent company, but also an attractive proposition for takeover by one or other of the main competitors in the sector. These were all private companies, two being SWFs, and they could benefit from the relative ease of acquisitions on the London market

DPW paid a high price for the acquisition, with a view to growing the company. Its chairman at the time was quoted as saying 'That's the only way the price we paid for the docks business makes sense. If the business stays as it is today, it is definitely not a good deal'. To date, this seems to have happened. Arguably private companies and SWFs are well placed for the major capital investment which the business needs.

DPW has added capacity fast, probably faster than its competitors. At the present time, it is likely to have to temper its expansionist strategy. International business press comments on need for restructuring and greater transparency in operations. In terms of employment and industrial relations, to date, there have not been major changes. However, there are concerns. These include concerns about ferries, pensions, and possible by-passing of trade unions.

First, P&O has long been one of Europe's largest shipping and ports companies and had already substantially restructured itself prior to being acquired by DPW. In many respects, DPW has built on this and carried forward policies which might have been pursued by the old management. Second, DPW is an interesting variant on the SWF model, being owned by a holding company which is itself owned by a sovereign state and which has a number of funds and companies under its umbrella. Third, DPW has taken major steps to integrate and develop the core part of the business, though top decision making has inevitably moved to Dubai. To date, there have not been negative effects on employment and industrial relations in the company, but there are concerns on the part of the unions which have been referred to above.

PART III: CONCLUSIONS

13 Conclusions from the case studies and lessons to be learned

Doing case studies is a popular and well established method of research in social science. The strength of this method is that things can be investigated in a real-life context and can be described in detail. On the other hand the main weakness is that generalizations beyond cases very similar to those studied usually cannot be made. Our study clearly shows the strengths and weaknesses of the case study approach. On the one hand, our case studies illustrate the complexity of the restructuring process on company level and allow us to construct different kinds of ideal types of restructuring situations. This is an advantage relative to large-scale quantitative studies which focus on net impact, but thereby ignore the heterogeneity of investment types and restructuring outcomes. On the other hand, the case study approach has limited generalizability, which makes it difficult to make statements regarding overall (net) impact of investor types on industrial restructuring. Our case studies also illustrated the complexity and difficulty of coming to a judgement about the impact of investment in specific cases – not only are many different indicators possible (profitability, employment, wages, sales growth; long versus short term), but also the necessary data on plant-level impact is difficult if not impossible to gather (especially in a matched comparison context).

In addition, we have tried to gather more evidence and research results from literature with case studies done by other researchers beyond the cases analysed in our sample. An overview on these materials can be found in the annex. In the following conclusions we intend to link our findings with the broader discussion on the business model impact of private equity, hedge funds and sovereign wealth funds. We hope that this method allows the reader to see more clearly the pattern of behaviour and the typical characteristics of the different investment funds and their possible influence on industrial restructuring.

13.1 Different level of market activities of PE, HF and SWF and different types of investments

The European statistics on private equity, hedge funds and sovereign wealth funds as they have been presented in the first part of this report show very clearly that the information available on the activities of the different types of funds is far from being complete. Especially for hedge funds and sovereign wealth funds this information is only

very fragmentary. There is a clear lack of transparency as all researchers and practitioners agree. Based on the existing data one can see that the level of activities and investments of PE, HF and SWF are very different in the six countries analysed. Investment by PE is by far the most important and widespread form in all six countries.

With some variation we found a large number of PE investments in all six countries, with the level of activities in Great Britain and France higher than in Germany, Spain and Italy. The investments of PE must be differentiated at least between early stage venture capital, development stage venture capital and buyout investments. In our case studies we analyse three PE cases: Dinosol in Spain, which has all the characteristics of a Mega Buyout, Marazzi in Italy, which is a development stage venture capital investment, and Zelmer in Poland, which is a mixture between buyout and development stage investment due to the very specific economic conditions in Poland after privatisation. The experience described in the case study on Cegelec in France also to some extent offers insights in PE activity. Before Cegelec was bought by an SWF investor it went through a phase of PE buyout.

The fast growing market for PE in all European countries during the last 10 years with a great volume of funds looking for attractive investments in a positive macroeconomic environment resulted in a rising number of risky investments. Therefore one can expect a decrease in the rate of returns on PE and a growing number of failed investments.

For the investments by HF research suffers from a lack of transparency but we believe that their direct investments combined with an approach as active investors in companies are not as widespread as is often supposed. In the majority of cases hedge funds operated as opportunistic investors holding only minority shares in companies without behaving as active shareholders. Our case study on KUKA is an example of this. A different story is the role of HF in buying distressed credits as in the case of Schefenacker.

The active investments by SWF are a more recent phenomenon which is concentrated on a few countries and branches. Here it is still early for any final judgement. However, they may well develop into very significant players.

13.2 Impact of investment strategies and type of funds

The three different investment vehicles follow distinct strategies in their investments. Depending on the concrete situation in which a fund invests, as well as on the type and main objective of the investment, the actual impact will be different. Our case studies show that the distinct business models of private equity, hedge funds and sovereign wealth funds influence their decisions and their strategic goals.

The most important differences are:

- ☐ main investment focus and the decision to become a majority owner or not
- ☐ investment horizon/duration and the willingness/desire to exit the investment short-term
- ☐ usage of leverage
- ☐ a link to other economic goals as in the case of sovereign wealth funds which often follow a long-term agenda which has not only financial but also national economic policy goals.

Our seven case studies show all these different approaches of investments funds in a nutshell. They also confirm the differences with regard to the role of these funds in different stages and situations of business development, e.g. a start-up situation, growth phases (Marazzi, Zelmer), merger and acquisitions (Schefenacker, Cegelec), turnaround and crisis situations (Schefenacker).

Finally, we have to differentiate between two different styles of investment behavior – passive and activist – which is also not necessarily connected to the different types of

funds. Though most sovereign wealth funds are regarded as rather "passive" investors with little direct involvement in management decisions, while private equity and hedge funds have much more activist investment styles, there is in reality also significant variation within all types of funds.

13.3 Situation of company and background of investment

Any conclusion on possible impacts on company development and on industrial restructuring will strongly depend on the concrete case one is analysing. Nevertheless, reviewing the seven cases and other case studies available one can identify "typical" behaviour and impacts of investments by PE and HF.

At the same time in many companies there are also specific economic constellations in which there seems to be hardly any difference regarding decisions for industrial restructuring between a company with PE or HF investments and one without.

In cases in which PE, HF or SWF have invested it is necessary to have a detailed analysis of the types and causes for the investment on the one side and for the reason of selling shares or accepting investments by PE, HF and SWF by the former owner. In many cases there was a "failure" in the governance structures of privately, publicly and state owned governance structures before the investment. There exist a broad range of possible constellations at the enterprise side:

- ☐ the investment could be motivated by financing constraints
- ☐ the company might have problems in introducing new technology and skill levels can be uncompetitive
- ☐ economies of scale might not be adequately exploited (e.g. through a conglomerate structure, focus on domestic market, etc.)
- ☐ unprofessional and/or entrenched management (e.g. in a family firm in the 2nd or 3rd generation of ownership)
- ☐ opportunities on the stock market due to an undervalued stock price might lead to short-term focus of investors
- ☐ a deficit in exploiting innovation potential

The case study of *Schefenacker* makes the importance of the specific background before the HF investment very clear. The crisis and the subsequent restructuring process of *Schefenacker* originally were not triggered by activities of financial investors. It was a result of an excessively risky growth strategy by the owner and the management of *Schefenacker*. The stripping of the company and the disposal of its parts to other industrial investors was a last move after a series of faulty decisions. In a way hedge funds in this case were the last option for *Schefenacker*, since without these investors the company would already have failed in 2005.

We can see a growing number of comparable cases since during the current financial crisis. Investors and companies who have used high leverage for a risky growth strategy are no longer able to fulfil their interest payments or repayment of principal and need fresh money.

Any comparison of case studies has to acknowledge these different areas where alternative investors could intervene. However, our cases show that, generally speaking, PE (and maybe SWF) can do much more than HF due to their ability to intervene "more deeply" in the company's structure. PE and SWF often buy the whole company and have as the majority owner greater possibilities for restructuring processes. HF on the other hand in most cases are more limited to "one off" improvements in value, e.g. through governance changes or spinning off non-core operations.

13.4 Typical PE

PE investments can be categorized in two business models. First, a typical investment linked to a growth strategy (as the cases of *Marrazzi* and also *Zelmer*). In these cases PE offers an opportunity to realize growth into new markets, which is risky and not realizable without risk capital. If the strategy works out and the economic performance is sufficiently high all partners involved end up with high returns on their investment.

The *Zelmer* case shows influence of private equity funds on a company which was formerly owned by the State. The old *Zelmer* management had not been able to develop and pursue a stable growth strategy. The PE investors helped to introduce changes and to adapt to market demands. The direct restructuring in terms of the number of employees and production sites was limited. The key instrument used by PE was to improve operational performance and to build on the strong value of an intangible asset, i.e. the well known brand name *Zelmer*.

The *Marazzi* Group seems to be a "virtuous case", at least until early 2008. The private equity funds enabled the already internationally active company to continue its course of expansion and consolidation.

Second, PE invests in an undervalued company with good growth potential, free cash flow and assets that can be capitalized for financial reengineering strategies (*Dinosol* and *Cegelec*). Cases like *Cegelec* and *Dinosol* are in many ways typical of PE activities. PE tries to invest in a company, use free cash flow and sale of assets to refinance at least part of the deal. Parallel to this is a period of restructuring the core business to improve the profitability of the company. Finally the PE fund tries to sale the company to another investor.

The *Dinosol* case shows clearly how a PE company works, setting financial parameters, but then devolving most aspects of management to local managers, many of whom are incumbent managers. Cases like *Dinosol* can end tragically for the company. This is especially the case if the PE investor sells the company after a first restructuring phase, leaving it equipped with fewer assets and more debt, to a new owner. This combination of low capital, frequent change in ownership, high cost of change management and complicated market environment is also part of the PE story.

In all cases PE investments are closely linked to an active restructuring policy of the funds and a well known bundle of instruments, including different forms of financial engineering to free up money for the PE investors.

13.5 Typical HF

HF are complicated to describe. Partly this is result of their lack of transparency. But partly it is also a consequence of their free style approach to investment. Our case studies of HF investments also show two different investments. In the first case we see an active investor initially making a short term investment at *KUKA*. This active investor with a minority of shares forced an undervalued company into a restructuring process. However, in the end the active investor retained their investment in *KUKA* for a long time and the management is now following a strategy similar to the one suggested by the active investor.

In the second case (*Schefenacker*), the entrance point for the HF was a failed high risk growth strategy pursued by the former family owner. The HF acquired a majority of the company by buying the defaulted loans of the former owner.

Although these cases are in a way typical for HF investments they do not cover all kinds of HF investments. Typical for HF are on the one hand short term investments in larger listed companies to realize short term profits. On the other hand there are a growing

number of HFs which invest in distressed debt. By doing this they offer other market participants like banks an opportunity to reduce their risks and exit investments with acceptable losses.

13.6 Typical SWF

The two SWF investments analysed show on the one hand the expected long term orientation of the investors and also the possible (but so far not proven) linkage strategy to national development goals of the investor. However, this does not cover the situation where SWFs take smaller ownership stakes in listed companies.

The case of *Cegelec* illustrates the acquisition of a company by a sovereign wealth fund after a period of ownership by several private equity funds. The sale to Qatari Diar offered a good exit opportunity for LBO France with high returns on its original investment. At the same time Qatari Diar offered a changed framework and new opportunities for *Cegelec* because Qatari Diar gives financial and structural stability to the firm and the company's potential and profitability is measured on a medium and long term scale.

The *P&O* case is another interesting variant on the SWF model, DPW being owned by a holding company which is itself owned by a sovereign state and which has a number of funds and companies under its umbrella. DPW has taken major steps to integrate and develop the core part of the business, though top decision making has inevitably moved to Dubai. To date, there have been no negative effects on employment and industrial relations in the company, despite concerns on the part of the unions.

13.7 Impact on restructuring – short term or long term effects?

Given the large differences between the cases any impact assessment on industrial restructuring and economic success of the companies has to be elaborated in a differentiated and cautious way. In fact, it is difficult to draw firm conclusions. First, there are no accepted criteria for measuring impact and success. Should one compare the development of profits, EBIT, EBITDA, stock market value or other micro-economic performance criteria? Even if this should be possible there remains the fact that, due to the investment and restructuring, the baseline for comparison does not exist any more. In the case of KUKA more than 10 subsidiaries have been sold during restructuring.

The case shows the catalytic effect active institutional investors can have on industrial change. However, because the impact assessment on industrial restructuring cannot be limited to the original company but also has to follow up on the development of all those divisions and companies which have been sold during the last years, it is simply not possible to present for example an estimate of whether in total a net increase or decrease in the number jobs resulted.

In any case the effects have to be analysed in a short term and a long term perspective. In our cases there have been short term impacts on wages as far as the companies underwent restructuring processes and economic problems. However, this is not specific to PE or HF activities, but rather apply to all restructuring situations. In general, the investors adapted to national rules and in most cases left the operational work to the management of the companies.

In a long term perspective at least PE activities as venture capital investors should lead to economic growth of the companies and creation of new jobs. The results will be more blurred in those cases where PE (or other investors) use their position as owners of the companies to withdraw capital and realize short term profits for the investor.

13.8 Impact on employment

The different circumstances in each case make it difficult to come to any conclusions regarding the impact on employment. If the investment by PE, HF or SWF is successful

and there is long term growth of the company one would expect a positive impact on employment figures. However, at least in some cases of investments by PE and HF, there exist some strong indications that the withdrawal of financial resources and the concentration on core business lead to job losses in company sites which are closed down or sold. Thus, acquisitions may lead to the closure or disposal of certain assets deemed not to be central.

Regarding wage developments and working conditions in the long term perspective we have no indications in our case studies that there is a negative impact. All impacts on wages we could observe were related to the poor economic performance of the company and not really specific to the fact that a PE or HF was invested. Regarding the impact on employment/wages another factor is decisive: how "deeply" are the alternative investors intervening in the company structure and also how high is the growth potential is at the target company.

For HF there seem to be fewer effects, since they do not intervene so deeply into operations. However, it is possible to find cases in which in the long run there is a strong pressure for cost saving and wages limitations for the company. This is especially the case if liquid resources are reduced through special dividends. For PE there seem to be more effects, but this could be in both the positive and the negative direction as the Zelmer case shows. On the one hand a large temporary work force was introduced at Zelmer. But on the other hand a successful growth strategy can lead to more job security and wage increases. In the cases we looked at employment reductions were not the "first choice" strategy of the investors - but of course the alternative investors want to make money and are generally "agnostic" about whether employment increases or falls.

13.9 Adaption to national rules and impact on social dialogue

In our cases the adaptation of the investors to national rules relates to all forms of social dialogue. In most cases the investors are not visible to the employee representatives, and local management is used to implement changes and new strategies. In two of our cases the investors were open to innovative solution to dilute the negative consequence of restructuring. At Schefenacker the strong position of the employee representatives provides a good example of the influence of external factors on the outcome of such restructuring processes. In fact, in this case institutional investors like hedge funds adapted to national industrial relations and social practices and agreed to a political solution. This saved most of the jobs at the successor company Odelo by using a transfer company. Although the hedge funds' investment strategy followed a classic restructuring model in the first phase, employee representatives had a quite influential position in the restructuring process and were able to avoid large scale dismissals and factory closings.

Similarly, developments in the case of Permira-DinoSol led to a situation where an investor in risk funds changed its normal habits (buy-streamline-restructure-sell) and introduced a sectoral business logic which includes a restructuring method that is innovative within the domestic context and socially responsible.

14 Summing up – positive and negative factors of investment funds on restructuring

Our case studies show a mixed picture. In some cases investors as HF or PE have a positive impact on company performance and restructuring processes. The PE industry repeats this argument continuously in public. These positive factors can be linked to the investments of all three types of funds. To name some of them:

- ☐ The funds make the risk-orientated financing of growth possible (as well as in research and access to new markets)
- ☐ They give liquidity in the market for change of ownership
- ☐ They intervene in companies and in the market to overcome encrusted structures and improve shareholder value,
- ☐ In some cases they strengthen the management capacities of companies.

In the case of active investors one could argue that this speeds up a process of value creation in the companies and even HF could say that their function of buying distressed credits can have positive impacts on the stability of the financial system.

Most of these impacts will only be realized in a long term perspective and can not be measured on a company case study level. In a way the activities of PE and HF remind one of the Schumpeter phrase of creative destruction as a characteristic part of capitalist market systems.

As far as the impacts of SWF are concerned some other positive factors could be important. One could postulate that SWF represent some new form of long term orientated "patient" capital which gives the companies additional resources and longer time periods for investments. Additionally new markets can be opened for companies like Cegelec. However, time has to prove whether these possibilities are ever realized.

On the other hand our case studies also give some insights on the "dark side" of these investors. There are clearly negative factors and dangers for companies and employees linked to the investments of PE, HF and SWF. Of course the dangers are that PE and HF are very dependent upon current market conditions for their business models:

- ☐ HF may be dependent upon market myopia (short term orientation) to realize short term gains
- ☐ PE (at least in leveraged deals) is dependent upon risk-friendly capital
- ☐ and now (especially the new PE funds focusing on distressed situations) are dependent upon the swing in the other direction -- e.g. risk aversion by forced selling by banks of securities at "undervalued" prices onto the market.

For PE investments the most obvious negative impacts on company development and industrial restructuring are directly linked to the economic goals of these investment vehicles. The whole PE economic story is about buying companies, restructuring them and selling them for a higher price. Between buying and selling is a phase of freeing financial resources. This can be done by financial re-engineering strategies like financing part of the purchase price as a loan to the company, capitalizing assets and withdrawing financial resources from the companies. The results are comparatively undercapitalized companies which run into severe economic problems as soon as the macro economic environment deteriorates. The consequence is also strong pressure on the employees as economic performance is not fulfilling the high expectations of the investors. In those cases where PE investors tried to realize risk minimizing short term strategies to re-finance their investment the negative impact of the long term performance will outweigh all other effects. The need for outsized profit is clearly a present danger for the PE business model.

For HF the negative impact factors are linked to the short term nature of their investments and their lack of transparency. Listed companies in particular can be victims of HF activities with the consequence of short term demands for restructuring which might weaken the economic potential and stability of the company. The problem of these kind of activities is that they redistribute financial resources from the industrial sector to the financial sector (and finally to wealthy investors).

For SWF the possible risks mainly are seen in their linkage to political goals of the states behind the funds. In fact, the practical knowledge and the transparency of these funds is so low that we can only guess what the positive or negative impact are.

In any case, transparency is clearly an issue and there is a real need for further research on this matter and an intensive political debate which should focus on the issue of transparency in the investments of these funds.

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ANNEX

Annex I: National data on PE, HF and SWF

France

Private Equity Summary Information

Investment and Fundraising Activity	2003	2004	2005	2006	2007
Investments (by domestic PE) (% of GDP)	0.27	0.36	0.43	0.57	0.66
Investments (in domestic firms) (% of GDP)				0.61	0.64
Fundraising (by domestic PE funds) (million EUR)	2038	2411	11451	10617	6551
Investments (by PE in domestic firms) (million EUR)		6359	7654	10798	11856
Investments (by domestic PE funds) (million EUR)	4246	5227	7294	10100	12288
- Seed	0.7%	0.7%	0.0%	0.0%	0.1%
- Startup	8.6%	7.2%	6.5%	5.3%	2.8%
- Expansion	23.8%	22.2%	12.8%	13.6%	9.4%
- Replacement	9.5%	2.2%	4.0%	1.2%	2.4%
- Buyout	57.4%	67.7%	76.7%	79.9%	84.7%

Source: European Private Equity and Venture Capital Association Yearbooks (various years)

Hedge Funds - Largest 20 Positions in Companies Listed in France (Dec 2008)

Security Name	Val (\$MM)	% Shares	Investor Name	% Portfolio
CGG Veritas	37.35	0.43	Zenit Fund	3.44
BNP Paribas	30.39	0.03	Zenit Fund	2.8
Cap Gemini	29.86	0.33	Zenit Fund	2.75
Ubisoft Entertainment SA	26.54	0.83	Advantage Advisers Xanthus Fund, L.L.C.	3.93
Societe Generale Paris	17.89	0.02	BBVA Durbana Int Fund BBVA Partners EUR Absolute Return	33.37
Sanofi Aventis	12.97	0.02	St James's Place Continental European Acc	5.73
Credit Agricole SA	12.45	0.03	St James's Place Continental European Acc	5.5
Total SA	12.27	0.01	St James's Place Continental European Acc	5.42
France Telecom SA	12.17	0.02	St James's Place Continental European Acc	5.38
Thales	11.56	0.12	St James's Place Continental European Acc	5.11
Bull SA	9.97	1.86	Futuris	3.99
EDF	9.61	0	Zenit Fund	0.89

Carrefour Supermarche SA	8.08	0.02	St James's Place Continental European Acc	3.57
EDF	8.07	0	Nordea European Equity Hedge	4.95
France Telecom SA	7.87	0.01	Bedlam Global Fund	5.49
Air Liquide	7.76	0.02	Handelsbanken Hedgefond Aktie Europa	11.77
Essilor International	5.65	0.05	St James's Place Continental European Acc	2.5
TF1	5.59	0.15	Bedlam Global Fund	3.9
Carrefour Supermarche SA	5.38	0.01	Pioneer Long/Short European Equity	5.78
Vivendi SA	5.38	0.01	Bedlam Global Fund	3.75

Source: Thomson Financial

Sovereign Wealth Funds - Largest 20 Positions in Firms Listed in France (Dec 2008)

Security Name	Val (\$MM)	% Shares	Investor Name	% Portfolio
Total SA	1,585.38	1.25	Norges Bank	1.04
Sanofi Aventis	874.39	1.05	Norges Bank	0.57
GDF Suez	684.21	0.64	Norges Bank	0.45
AXA SA	590.68	1.28	Norges Bank	0.39
France Telecom SA	547.65	0.75	Norges Bank	0.36
BNP Paribas	535.24	1.4	Norges Bank	0.35
Vivendi SA	476.45	1.26	Norges Bank	0.31
Groupe Danone	422.74	1.37	Norges Bank	0.28
Societe Generale Paris	390.97	1.35	Norges Bank	0.26
Carrefour	354.99	1.32	Norges Bank	0.23
L Oreal	288.27	0.56	Norges Bank	0.19
Vinci SA	282.17	1.36	Norges Bank	0.19
Air Liquide	269.05	1.13	Norges Bank	0.18
Vivendi SA	250.51	0.66	Abu Dhabi Investment Co.	7.65
EDF	216.32	0.21	Norges Bank	0.14
Schneider Electric	215.61	1.18	Norges Bank	0.14
Saint-Gobain SA	214.33	0.94	Norges Bank	0.14
Veolia Environnement SA	201.85	1.38	Norges Bank	0.13
Alstom	197.51	1.18	Norges Bank	0.13
LVMH Moet Hennessy Lou Vuitton SA	182.12	0.56	Norges Bank	0.12

Source: Thomson Financial

Italy

Private Equity Summary Information

Investment and Fundraising Activity	2003	2004	2005	2006	2007
Investments (by domestic PE) (% of GDP)	0.23	0.11	0.15	0.23	0.10
Investments (in domestic firms) (% of GDP)				0.33	0.21
Fundraising (by domestic PE funds) (million EUR)	1937	1663	1345	2275	2408
Investments (by PE in domestic firms) (million EUR)		1861	2882	4916	3173
Investments (by domestic PE funds) (million EUR)	3034	1480	2186	3415	1459
- Seed	0.2%	0.3%	0.2%	0.1%	0.0%
- Startup	1.7%	1.2%	1.1%	0.7%	0.8%
- Expansion	19.2%	30.9%	18.9%	28.3%	9.8%
- Replacement	4.4%	5.6%	10.1%	4.8%	1.8%
- Buyout	74.4%	61.9%	69.7%	66.0%	87.6%

Source: European Private Equity and Venture Capital Association Yearbooks (various years)

Hedge Funds - Largest 20 Positions in Companies Listed in Italy (Dec 2008)

Security Name	Val (\$MM)	% Shares	Investor Name	% Portfolio
Parmalat SpA	107.56	1.63	Zenit Fund	9.92
Benetton Group SpA	75.71	2.29	Zenit Fund	6.98
Unicredit SpA	41.78	0.03	Zenit Fund	3.85
Intesa Sanpaolo SpA	27.61	0.03	RIT Capital Partners Trust	6.94
Unicredit SpA	23.27	0.02	BBVA Durbana Int Fund BBVA Partners EUR Absolute Return	43.4
Enel Societa Per Azioni	12.79	0.03	Evergreen Utility and Telecom Fund	3.55
ENI SpA	8.91	0.01	St James's Place Continental European Acc	3.94
A2A SpA	8.52	0.11	St James's Place Continental European Acc	3.77
Banca Popolare di Milano	8.39	0.15	Zenit Fund	0.77
Saipem SpA	7.20	0.03	Nordea European Equity Hedge	4.41
Autogrill SpA	5.91	0.14	Pioneer Long/Short European Equity	6.35
Parmalat SpA	4.50	0.07	Pioneer Long/Short European Equity	4.83
Fiat SpA Ordinary	4.34	0.02	Nordea European Equity Hedge	2.66

Impregilo SpA	3.79	0.25	St James's Place Continental European Acc	1.67
Dada SpA	3.68	0.95	Zenit Fund	0.34
Assicurazioni Generali SpA	3.35	0.01	Pioneer Long/Short European Equity	3.6
Davide Campari-Milano SpA	3.33	0.12	Pioneer Long/Short European Equity	3.58
Mediobanca SpA	3.12	0.02	Pioneer Long/Short European Equity	3.35
IMMSI SpA	2.86	0.44	Pioneer Long/Short European Equity	3.08
ENI SpA	2.51	0.01	OKO Equity Hedge	5.22

Source: Thomson Financial

Sovereign Wealth Funds - Largest 20 Positions in Firms Listed in Italy (Dec 2008)

Security Name	Val (\$MM)	% Shares	Investor Name	% Portfolio
ENI SpA	831.23	0.88	Norges Bank	0.55
Intesa Sanpaolo SpA	453.83	1.07	Norges Bank	0.3
Unicredit SpA	384.87	1.09	Norges Bank	0.25
Assicurazioni Generali SpA	380.18	0.98	Norges Bank	0.25
Telecom Italia SpA	335.54	1.54	Norges Bank	0.22
Enel Societa Per Azioni	315.86	0.8	Norges Bank	0.21
Atlantia SpA	151.51	2.02	Norges Bank	0.1
Unione Di Banche Italiane SCPA	111.07	1.19	Norges Bank	0.07
Mediaset SpA	107.60	2.04	Abu Dhabi Investment Company	3.29
Fondiaria-Sai	83.81	3.72	Norges Bank	0.06
Banca Monte Dei Paschi Di Siena	71.09	0.6	Norges Bank	0.05
Saipem SpA	65.71	0.89	Norges Bank	0.04
A2A SpA	65.12	1.16	Norges Bank	0.04
Banco Popolare Societa Cooperativa	58.85	1.31	Norges Bank	0.04
Fiat SpA Ordinary	54.80	0.77	Norges Bank	0.04
Mediobanca SpA	53.40	0.59	Norges Bank	0.04
Alleanza Assicurazioni SpA	44.93	0.65	Norges Bank	0.03
ERG SpA	40.44	2.04	Norges Bank	0.03
Buzzi Unicem SpA	35.58	1.31	Norges Bank	0.02
Parmalat SpA	32.45	1.16	Norges Bank	0.02
Luxottica Group SpA	29.19	0.35	Norges Bank	0.02

Source: Thomson Financial

Germany

Germany - Private Equity Summary Information

Investment and Fundraising Activity	2003	2004	2005	2006	2007
Investments (by domestic PE) (% of GDP)	0.12	0.17	0.12	0.15	0.31
Investments (in domestic firms) (% of GDP)				0.31	0.44
Fundraising (by domestic PE funds) (million EUR)	1191	1983	2875	2819	5662
Investments (by PE in domestic firms) (million EUR)		5119	5540	7227	10595
Investments (by domestic PE funds) (million EUR)	2481	3766	2695	3518	7452
- Seed	1.1%	0.6%	0.2%	0.9%	0.5%
- Startup	10.7%	8.8%	11.1%	6.6%	3.7%
- Expansion	16.6%	16.2%	35.7%	19.2%	6.7%
- Replacement	0.2%	3.0%	0.2%	2.8%	5.1%
- Buyout	71.5%	71.3%	52.8%	70.5%	83.9%

Source: European Private Equity and Venture Capital Association Yearbooks (various years)

Hedge Funds - Largest 20 Positions in Companies Listed in Germany (Dec 2008)

Security Name	Val (\$MM)	% Shares	Investor Name	% Portfolio
Arcandor AG	49.67	0.82	Zenit Fund	4.58
SAP AG	21.42	0.03	Futuris	8.57
Tui AG	18.08	0.26	Futuris	7.23
RWE AG (Neu)	15.45	0.03	St James's Place Continental European Acc	6.83
Deutsche Boerse AG	14.76	0.08	Advantage Advisers Xanthus Fund	2.19
Deutsche Telekom AG	14.30	0.02	St James's Place Continental European Acc	6.32
Deutsche Boerse AG	12.95	0.03	SGAM AI Eq Fd - Caxton Equity	2.94
Software AG Darmstadt	10.34	0.64	St James's Place Continental European Acc	4.57
E.ON AG	8.35	0.01	Zenit Fund	0.77
E.ON AG	8.31	0.01	Nordea European Equity Hedge	5.09
BAYWA	8.21	0.89	St James's Place Continental European Acc	3.63
Rheinmetall AG	8.00	0.28	Zenit Fund	0.74
Bayer AG	7.88	0.01	Bedlam Global Fund	5.5

Commerzbank AG	7.72	0.02	Futuris	3.09
Commerzbank AG	7.55	0.02	Zenit Fund	0.7
Siemens AG	6.64	0.01	Bedlam Global Fund	4.63
MAN AG	6.46	0.03	Nordea European Equity Hedge	3.96
Deutsche Telekom AG	6.08	0.01	Evergreen Utility and Teleco Fund	1.69
Volkswagen AG Preferred	5.90	0.04	Nordea European Equity Hedge	3.61
Continental AG	5.41	0.02	Pioneer Long/Short European Equity	5.81

Source: Thomson Financial

Sovereign Wealth Funds - Largest 20 Positions in Firms Listed in Germany (Dec 2008)

Security Name	Val (\$MM)	% Shares	Investor Name	% Portfolio
Daimler AG	1,854.60	6.90	Kuwait Investment Office	24.2
E.ON AG	1,287.67	1.6	Norges Bank	0.85
Siemens AG	887.83	1.3	Norges Bank	0.58
Deutsche Telekom AG	783.85	1.18	Norges Bank	0.51
Allianz SE	676.69	1.41	Norges Bank	0.44
Bayer AG	601.92	1.34	Norges Bank	0.4
RWE AG (Neu)	496.49	1.05	Norges Bank	0.33
BASF SE	450.64	1.24	Norges Bank	0.3
SAP AG	421.87	0.96	Norges Bank	0.28
Daimler AG	404.88	1.01	Norges Bank	0.27
Muenchener Rueckversicherung	378.95	1.17	Norges Bank	0.25
Volkswagen AG	370.96	0.36	Norges Bank	0.24
Deutsche Bank AG	273.84	1.12	Norges Bank	0.18
Deutsche Boerse AG	260.78	1.81	Norges Bank	0.17
Linde AG	199.89	1.4	Norges Bank	0.13
Deutsche Post AG	190.51	0.94	Norges Bank	0.13
Gea Group AG	160.85	8.21	Kuwait Investment Office	2.1
Continental AG	153.33	2.22	Norges Bank	0.1
Fresenius SE	151.65	3.2	Norges Bank	0.1
Henkel Ag &Co. Kgaa	144.60	2.1	Norges Bank	0.09

Source: Thomson Financial

Great Britain

UK - Private Equity Summary Information

Investment and Fundraising Activity	2003	2004	2005	2006	2007
Investments (by domestic PE) (% of GDP)	0.85	1.10	1.33	2.20	1.69
Investments (in domestic firms) (% of GDP)				1.26	1.03
Fundraising (by domestic PE funds) (million EUR)	14991	10057	45644	74993	41413
Investments (by PE in domestic firms) (million EUR)		9670	11860	23478	20897
Investments (by domestic PE funds) (million EUR)	13539	19086	23832	40897	34224
- Seed	0.2%	0.1%	0.1%	3.8%	0.1%
- Startup	4.4%	4.2%	3.4%	10.2%	2.2%
- Expansion	14.5%	14.6%	18.4%	12.7%	15.3%
- Replacement	11.0%	1.8%	5.3%	6.1%	5.6%
- Buyout	69.9%	79.3%	72.8%	67.2%	76.5%

Source: European Private Equity and Venture Capital Association Yearbooks (various years)

Hedge Funds - Largest 20 Positions in Companies Listed in the UK (Dec 2008)

Security Name	Val (\$MM)	% Shares	Investor Name	% HF Portfolio
PayPoint Plc	69.20	9.13	RIT Capital Partners Trust	17.39
Anglo American Plc	50.29	0.05	Genesis Emerging Markets Fund Limited	7.52
Bluebay Asset Management Ltd	23.53	1.76	RIT Capital Partners Trust	5.91
Tullow Oil Plc	22.54	0.15	Genesis Emerging Markets Fund Limited	3.37
British Sky Broadcasting Group Plc	22.14	0.11	RIT Capital Partners Trust	5.56
AstraZeneca Plc	17.90	0.03	Aktie Ansvar Graal Fonds	3.01
KGHM Polska Miedz SA	10.58	0.06	Eastern European Fund	3.38
AstraZeneca Plc	8.74	0.01	Catella Hedgefond	2.75
Diageo Plc	7.64	0.01	Handelsbanken Hedgefond Aktie Europa	11.58
Novatek OAO	7.41	0.01	Eastern European Fund	2.37
AstraZeneca Plc	7.26	0.01	Erik Penser Hedgefond	7.84
BT Group Plc	6.94	0.03	Bedlam Global Fund	4.84
BHP Billiton Plc	6.24	0.01	Global Emerging Markets Fund	0.64
X5 Retail Group NV	5.87	0.26	Genesis Emerging Markets Fund Limited	0.88

Reckitt Benckiser Group Plc	5.45	0.01	Handelsbanken Hedgefond Aktie Europa	8.26
Johnson Matthey Plc	5.03	0.07	Handelsbanken Hedgefond Aktie Europa	7.63
PIK Group OJSC	4.89	0.04	Eastern European Fund	1.56
Wolseley Plc	4.83	0.03	Handelsbanken Hedgefond Aktie Europa	7.32
BG Group Plc	4.63	0.01	Nordea European Equity Hedge	2.84
Prosperity Minerals Holdings Ltd	4.60	1.27	Waverton Asia Pacific Fund	3.48

Source: Thomson Financial

Sovereign Wealth Funds - Largest 20 Positions in UK Listed Companies (Dec 2008)

Security Name	Val (\$MM)	% Shares	Investor Name
Standard Chartered Plc	4,431.73	18.79	Temasek Holdings Pte. Ltd.
Sainsbury J Plc	2,979.83	27.19	Qatar Investment Authority
BP Plc	2,325.22	1.75	Kuwait Investment Office
Royal Dutch Shell Plc	2,162.22	3.23	Norges Bank
BP Plc	1,908.61	1.26	Norges Bank
Barclays Plc	1,677.16	5.82	Qatar Investment Authority
HSBC Holdings Plc	1,496.26	0.92	Norges Bank
Vodafone Group Plc	1,254.05	1.28	Norges Bank
GlaxoSmithKline Plc	1,196.98	1.25	Norges Bank
London Stock Exchange Group	848.92	15.26	Qatar Investment Authority
BG Group Plc	679.90	1.41	Norges Bank
Royal Dutch Shell Plc	625.05	0.71	Government of Singapore Investment Corp.
BHP Billiton Plc	554.08	1.38	Norges Bank
British American Tobacco Plc	411.85	0.79	Norges Bank
AstraZeneca Plc	405.05	0.75	Norges Bank
Reckitt Benckiser Group Plc	398.49	1.52	Norges Bank
Unilever Plc	383.22	1.3	Norges Bank
BG Group Plc	366.64	0.76	Government of Singapore Investment Corp.
British Land Co Plc	362.19	4.26	Government of Singapore Investment Corp.
Imperial Tobacco Group Plc	357.53	1.33	Norges Bank

Source: Thomson Financial

Poland

Poland - Private Equity Summary Information

Investment and Fundraising Activity	2003	2004	2005	2006	2007
Investments (by domestic PE) (% of GDP)	0.07	0.07	0.06	0.11	0.19
Investments (in domestic firms) (% of GDP)				0.21	0.24
Fundraising (by domestic PE funds) (million EUR)	26	304	59	937	571
Investments (by PE in domestic firms) (million EUR)		122	120	528	747
Investments (by domestic PE funds) (million EUR)	133	130	154	294	571
- Seed	11.3%	0.0%	0.0%	0.4%	0.3%
- Startup	1.6%	0.0%	0.3%	0.4%	0.1%
- Expansion	30.3%	20.1%	2.8%	5.2%	17.3%
- Replacement	32.1%	54.0%	64.6%	2.1%	0.1%
- Buyout	24.7%	25.9%	32.3%	91.9%	81.9%

Source: European Private Equity and Venture Capital Association Yearbooks (various years)

Hedge Funds - Largest Positions in Companies Listed in Poland (Dec 2008)

Security Name	Val (\$MM)	% Shares	Investor Name	% Portfolio
Telekomunikacja Polska SA	7.14	0.07	Eastern European Fund	2.28
KGHM Polska Miedz SA	6.90	0.07	Eastern European Fund	2.2
Telekomunikacja Polska SA	6.87	0.05	Bedlam Global Fund	4.79
Bank Polska Kasa Opieki Grupa Pekao	4.08	0.02	Eastern European Fund	1.3
Telekomunikacja Polska SA	2.81	0.03	Global Emerging Markets Fund	0.29
KGHM Polska Miedz SA	1.03	0.01	Global Emerging Markets Fund	0.11
Asseco Poland SA	0.47	0.02	Clariden Leu (Gue) Emerging Markets Equity Fund	0.96
Telekomunikacja Polska SA	0.47	0.01	Bedlam Emerging Markets Fund	8.31
Telekomunikacja Polska SA	0.46	0.01	Bedlam Europe Funds Plc Europe Fund	4.59
Reinhold Polska AB	0.22	0.4	FIM Maltti Hedge Fund	1.49
Raciborska Fabryka Kotlow SA Rafako	0.20	0.08	Vitruvius Capital Opportunities	0.66
Kopex	0.16	0.02	Vitruvius Capital Opportunities	0.54
Sygnity SA	0.12	0.07	Luxcellence Polunin Emerging Markets Technology FD	0.29

Source: Thomson Financial

Sovereign Wealth Funds - Largest 20 Positions in Firms Listed in Poland (Dec 2008)

Security Name	Val (\$MM)	% Shares	Investor Name	% Portfolio
Powszechna Kasa Oszczednosci Bank Polski SA	76.16	0.64	Norges Bank	0.05
Bank Polska Kasa Opieki Grupa Pekao	57.07	0.51	Norges Bank	0.04
Telekomunikacja Polska SA	56.57	0.65	Norges Bank	0.04
Polski Koncern Naftowy Orlen SA	35.25	0.95	Norges Bank	0.02
KGHM Polska Miedz SA	13.95	0.74	Norges Bank	0.01
Bank Zachodni Wbk	13.25	0.49	Norges Bank	0.01
TVN SA	10.74	0.68	Norges Bank	0.01
BRE Bank SA	10.10	0.51	Norges Bank	0.01
Globe Trade Centre SA	8.48	0.75	Norges Bank	0.01
PBG	7.97	0.9	Norges Bank	0.01
Polimex Mostostal SA	4.66	0.97	Norges Bank	0.01
Grupa Lotos SA	4.04	0.88	Norges Bank	0.01
Getin Holding SA	3.99	0.33	Norges Bank	0.01
Bank Handlowy W Warszawie SA	3.31	0.16	Norges Bank	0.01
Bioton SA	3.07	1.49	Norges Bank	0.01
Bank Millennium SA	2.12	0.26	Norges Bank	0.01
Agora	1.97	0.66	Norges Bank	0.01
Cersanit Krasnystaw SA	1.35	0.2	Norges Bank	0.01
Grupa Kety SA	0.92	0.49	Norges Bank	0.01
Polnord SA	0.46	0.26	Norges Bank	0.01

Source: Thomson Financial

Spain

Spain - Private Equity Summary Information

Investment and Fundraising Activity	2003	2004	2005	2006	2007
Investments (by domestic PE) (% of GDP)	0.18	0.25	0.29	0.29	0.29
Investments (in domestic firms) (% of GDP)				0.37	0.40
Fundraising (by domestic PE funds) (million EUR)	879	1577	1020	2884	3298
Investments (by PE in domestic firms) (million EUR)		2289	4299	3581	4226
Investments (by domestic PE funds) (million EUR)	1337	1967	2662	2815	3053
- Seed	0.5%	0.3%	0.3%	1.1%	0.1%
- Startup	3.7%	3.2%	4.1%	8.3%	3.2%
- Expansion	66.3%	60.4%	24.5%	23.4%	24.7%
- Replacement	1.9%	1.9%	1.2%	11.2%	6.1%
- Buyout	27.6%	34.2%	69.9%	55.9%	65.8%

Source: European Private Equity and Venture Capital Association Yearbooks (various years)

Hedge Funds - Largest 20 Positions in Companies Listed in Spain (Dec 2008)

Security Name	Val (\$MM)	% Shares	Investor Name	% Portfolio
Cintra Concesiones de Infraestructuras Transporte	44.77	0.54	Zenit Fund	4.13
Gamesa Corporacion Tecnologica SA	17.01	0.21	Advantage Advisers Xanthus Fund	2.52
Grupo Ferrovial SA	15.57	0.16	Zenit Fund	1.44
Banco Santander SA	7.76	0.01	Zenit Fund	0.72
Telefonica SA	5.88	0.01	BBVA Durbana Int. Fund	10.86
Union Fenosa SA	5.47	0.03	Nordea European Equity Hedge	3.35
Banco Popular Espanol SA	5.42	0.02	Handelsbanken Hedgefond Aktie Eur	8.21
Bolsas y mercados	4.96	0.23	Advantage Advisers Xanthus Fund	0.74
Repsol YPF SA	4.07	0.01	Nordea European Equity Hedge	2.49
Fomento de Construcciones SA	3.78	0.04	Zenit Fund	0.35
Banco Bilbao Vizcaya Argentaria SA	3.44	0.01	Pioneer Long/Short European Equity	3.69
Red Electrica Corp	2.55	0.04	Evergreen Utility and Teleco Fund	0.71
Acerinox SA	1.88	0.03	BBVA Durbana Int. Fund	3.46
Banco Santander SA	1.74	0.01	BBVA Durbana Int. Fund	3.21

Telefonica SA	1.72	0.01	Templeton Global Long-Short Fund	1.45
Inditex	1.66	0.01	Nordea European Equity Hedge	1.02
Promotora De Infom	1.60	0.04	Nordea European Equity Hedge	0.98
Bolsas y mercados	1.55	0.03	Zenit Fund	0.14
Banco Bilbao Vizcaya Argentaria SA	1.38	0.01	BBVA Durbana Int. Fund	2.55
Telefonica SA	1.28	0.01	Waverton Continental European Fund	3.9

Source: Thomson Financial

Sovereign Wealth Funds - Largest 20 Positions in Firms Listed in Spain (Dec 2008)

Security Name	Val (\$MM)	% Shares	Investor Name	% Portfolio
Telefonica SA	1,283.83	1.22	Norges Bank	0.84
Banco Santander SA	952.73	1.22	Norges Bank	0.63
Banco Bilbao Vizcaya Argentaria SA	579.12	1.26	Norges Bank	0.38
Iberdrola SA	567.84	1.23	Norges Bank	0.37
Repsol YPF SA	318.11	1.22	Norges Bank	0.21
Union Fenosa SA	174.65	0.76	Norges Bank	0.11
ACS Actividades Construcciones Servicios	136.34	0.93	Norges Bank	0.09
Gas Natural Sdg SA	134.67	1.1	Norges Bank	0.09
Inditex	129.89	0.47	Norges Bank	0.09
Enagas SA	127.11	2.42	Norges Bank	0.08
Banco De Sabadell SA	122.26	1.21	Norges Bank	0.08
Banco Popular Espanol SA	112.82	1.08	Norges Bank	0.07
Criteria CaixaCorp SA	70.66	0.54	Norges Bank	0.05
Grifols SA	66.24	1.79	Norges Bank	0.04
Abertis Infraestructuras SA	62.06	0.52	Norges Bank	0.04
Iberdrola Renovables SA	60.63	0.33	Norges Bank	0.04
Acciona SA	52.84	0.66	Norges Bank	0.03
Acerinox SA	44.52	1.09	Norges Bank	0.03
Indra Sistemas SA	43.67	1.2	Norges Bank	0.03
Gamesa Corporacion Tecnologica SA	38.26	0.87	Norges Bank	0.03

Source: Thomson Financial

Annex II: Overview on other available case studies

Company based case studies on the impact of PE, HF and SWF on working conditions and labour relations

Company	Background of PE, HF, SWF involvement	Major findings with regard to the impact on working conditions and labour relations	Source
Autoteile Unger	In 2002 the company's founder, Peter Unger, sold his majority stake to the PE company Doughty Hanson & Co, due to the missing of a successor and necessity for liquid assets. In 2004 the PE fund KKR acquired major stakes by a secondary buy-out.	Both investors have changed the accounting and financing structure of the company considerable. Additionally KKR has influenced the company's internal structure. Board members has been removed, an extensive reporting system has been installed and stringent targets for the employees has been introduced. Furthermore the working week has been lengthened from 37.5 to 40 hours.	Van den Burg / Rasmussen (2007)
Beru	In 1997 Beru was floated to the stock market. 2001 the Carlyle Group invested in the company. Originally Carlyle planned to fully take over Beru but in the end they were only able to acquire a 35% stake.	Beru show a constant growth rate which correlates also with a steady increase in their working force (7.2% p.a.)	Faber (2006)
Bulgarian Tele-communications Company	After a two-year privatisation process in 2004 Advent International acquired a 65% stake in the company. Since BTC went partly public in 2005 several investment firms hold minority stakes. In December 2005 the Icelandic company Novator took over 85% of BTC. In 2007 Novator sold BTC to the US investment group AIG.	Due to a controversial agreement by the government the privatisation process already has been slashed employee number and social dialogue has broken down. In the first year of the transfer to equity ownership BTC the workforce was reduced by nearly 10,000 jobs out of a workforce of 24,392 workers in 2002. In 2005 further 3,500 workers became redundant. Against a weak social dialogue a social partnership agreement was only agreed in 2006 after complaints from ETUC and UNI-Europe and sustained pressure from the local unions a social partnership agreement was finally agreed in 2006.	Van den Burg / Rasmussen (2007)
Deutsche Börse	In 2001 the German Stock Exchange was itself floated to the stock market. At that time 68% of the shares were owned by German investors. In 2005 this ration has changed into a 93% foreign ownership structure, also consisting of several hedge funds like TCI, Atticus and Capital Group	The mentioned hedge funds mainly influenced the operative business of Deutsche Börse. They inhibited a second attempt to take over the London Stock Exchange in 2005 and forced CEO Seifert to step down the management board. Significant impacts concerning employment issues are not known.	Van den Burg / Rasmussen (2007)

DIS (Deutsche Industrie Service AG)	In 2006 the Swiss recruitment agency Adecco launched a takeover bid for their business rival DIS. Adecco finally was able to acquire 83% of the shares in DIS. While two hedge funds Elliot Int. and Liverpool Lmt. acquired 10% respectively 3% of the shares.	Adecco planed to delist DIS but failed due to the resistance of the other shareholders. As a reaction Adecco tried to purchase more stakes from the minority shareholders but failed again. The strategy of the HF was designed to ensure that Adecco bought of their resistance with a considerably higher settlement offer, so that the HF could make a substantial profit. Significant impacts concerning employment issues are not known.	Van den Burg / Rasmussen (2007)
DT-Group	The Danish wood importer and producer of building materials DT-Group was bought by the PE group CVC in 2003. In 2006 CVC sold the DT-Group to the British building materials provider Wolsely plc.	The numbers of employees increased by 10%, but this is only because of acquisitions of formerly private owned building markets.	Van den Burg / Rasmussen (2007)
Edscha	In 1997 the former manager of Edscha Kuschetzki backed by two PE company's take over the company (MBO). In March 1999 Edscha went public. The company developed well and in 2002 the PE investors decided to exit and sold their stakes to the US investor Carlyle. With a squeeze-out Carlyle acquired the hole company and delisted Edscha in January 2004. From that time on the company's performance decreased and in February 2009 Edscha went insolvent.	After the first MBO Edscha developed quite well and constantly increased it's working force (from 3,811 employees in 1997 to 5,044 employees in 2001). After the Carlyle group started their investment in Edscha the company's performance decreased and therewith the number of employees. Since October 2006 around 500 jobs were lost at Edscha.	Blome-Drees / Rang (2006)
Eircom	The former state-owned telecommunication company was went public in 1999 and beside a large proportion of citizens also a union lead coalition acquired a 14.9% stake in the company. In 2001 a consortium headed by Valentina bought the company and took it private again. During this transaction the employees raised their stakes to 29.9%. Three years later Valentina exit and Eircom went public again. Till March 2006 the investment fund Babcock & Brown (BCM) acquired a 27.1% stake. Together with the employee coalition BCM made an offer for the remaining minority shares. The bid was successful and today the employees hold a 35% stake in the company with BCM controlling the rest.	Since the Eircom went public for the first time a reduction in the workforce was realized, achieved by the company offering voluntary redundancy and early retirement schemes. Increased automation and competition balanced with a reduction in revenues and a challenging regulatory regime have set the pace on the agenda. Due to the employee participation unions were able to negotiated guarantees for the existing employment conditions, including safeguarding of pensions. All agreements will also be honoured in accordance with existing industrial relation provisions.	Van den Burg / Rasmussen (2007)

Frans Bonhomme	Since 1994 the company has undergone four LBOs. In 1994 Fonds Partenaires bought the company. Later in 2000 Frans Bonhomme was acquired in a second LBO by a consortium of several institutional investors like Cinven, PAI and Astord Partners. In June 2003 Apax Partners and PE funds of Goldman Sachs bought the company. Finally in October 2005 again Cinven acquired Frans Bonhomme from Apax.	Thanks to the PE investors Frans Bonhomme has succeeded in achieving a significant international expansion which was followed by an increase in employment level.	Van den Burg / Rasmussen (2007)
Friedrich Grohe AG	In 1999 the members of the Grohe family sold their majority stakes to an investment group headed by the British PE company BC Partners. In May 2004 the two PE firms Texas Pacific and Credit Swiss First Bond acquired Grohe in a secondary buy-out.	Under the first PE investor BC Partners Grohe developed quite well: further progress was made in internationalising the company, its organisational structure was modernised, new products were put on the markets, the product range was diversified, and R&D expenditures were increased. In contrast the second PE investor shift a larger part of its production to low-wage, which leads to job cut backs in Germany and a damage of the prestigious brand Grohe. During the restructuring process the second PE company's play of the various locations and workforces against each other. Due to the intervention of the works councils and a general good going business in Germany finally "only" 770 workers lost their jobs.	Van den Burg / Rasmussen (2007)
Gate Gourmet	In 2002 the PE company Texas Pacific acquired Gate Gourmet and delisted the company.	Workers at Gate Gourmet have experienced severe job cuts since being acquired by Texas Pacific. Since 2002 the workforce has been reduced from 26,000 to 20,000 workers. Furthermore the PE fund sought severe wage reductions and stricter agreements concerning working hours, holiday leave and shift pay. These actions caused union strikes in Great Britain and Germany.	Van den Burg / Rasmussen (2007)
Grohe AG	In 1999 the members of the Grohe family sold their majority stakes to an investment group headed by the British PE company BC Partners. In May 2004 the two PE firms Texas Pacific and Credit Swiss First Bond acquired Grohe in a secondary buy-out.	Under BC Partners Grohe developed quite successful. R&D and investments were expanded, operations improved and the workforce staid stable. After the selling to Texas Pacific and Credit Swisse the situation changed rapidly. The new investors forced the management out and assigned McKinsey to reduce costs. Due to their recommendation Grohe undertake a severe reduction of their workforce and cut their range of products.	Schewe (2009)
Hugo Boss AG	In 2007 the PE company Permira took over Hugo Boss for € 3.2 billion. At that time this deal was the biggest PE-deal in the European luxury fashion sector.	In 2008 the company paid out a € 450 million dividend, three times more than the 2007 net income. Permira recieved around € 350 million. The companys workcouncil fear a longterm financial weakening of the company.	Schewe (2008)

ISS Denmark	In 2005 ISS was bought by the two PE funds EQT and Goldman Sachs Capital Partners.	The ISS Group is known for its social responsibility concerning their workforce. Most of the employees in Denmark had shares in the company and preferred the LBO. Further impacts on working conditions and labour relations are not known.	Van den Burg / Rasmussen (2007)
Kabel Deutschland	In March 2003 an investor group consisting of Apax, Providence and Goldman Sachs took over the company.	Although exact figures about the employment development are missing, other operating figures show indirectly an increase in the number of employees (EBITDA per employee / Sales per employee).	Faber (2006)
Linde	After the break up of the so called Deutschland AG, Linde became an interesting target for institutional investors. Today 69% of the shares of Linde are owned by institutional investors.	In 2003 Linde sold their refrigeration business to the US group Carrier, which leads to massive job cuts in this area. Working time has been lengthened and made more flexible and more shifts have been introduced to improve the utilisation of the company's assets. In 2006 Linde took over the British competitor BOC and sourced out several parts of both company's. Regarding the materials-handling section KION the German works councils and the IG Metall negotiated an employment guarantee until 2011. The employee representative have forced that this agreement be also valid for any purchaser if it was sold.	Van den Burg / Rasmussen (2007)
Märklin	The sale of Märklin to a PE company was mainly made under pressure from the banks to which the company owned money. After disputes between the owner family and the banks, the company finally was sold to the British PE firm Kingsbridge in 2006.	Before the acquisition by Kingsbridge, Märklin already had dismissed 340 employees in 2004. In 2007 further 340 jobs were cut at three German locations. In February 2009 the company couldn't handle the constant losses and went insolvent. Due to this further 370 employees were dismissed.	Van den Burg / Rasmussen (2007)
Messer Griesheim	In 2002 the PE investors Goldman Sachs and Alliance Capital Partners acquired a 67% stake in Messer Griesheim. In January 2004 two-third of Messer Griesheim were sold to the French competitor Air Liquide. The PE investors sold their stakes to the owner family, who continued with the remained one-third.	Private equity investors had little to no contact with the employees. Nevertheless the situation for the employees stays stable after the investment. No contracts were changed, resources for employee development were expanded and strategic information's were circulated. The deal introduced an innovative employee incentive programme.	World Economic Forum (2008)
Mobilcom	In 2000 France Telecom acquired a 28.5% stake in the company. After financial troubles and constantly rising debts, in 2005 France Telecom sold 27.3% of their stakes to the US investor Texas Pacific Group.	Significant impacts concerning employment issues are not known.	Van den Burg / Rasmussen (2007)

MTU Aero Engines	In 2003 the former owner Daimler-Benz sold the aerospace division of MTU to the US investor KKR. After floated the company at the stock market, KKR exit in January 2006.	Employee representatives emphasise that they are more involved after the KKR investment. Due to representatives of KKR the interaction between employees and employers was enhanced	Scheytt (2006), Mitbestimmung 06/2006
New Look	In April 2004 Apax Partners and Permira each invested £ 100 million in a buy-out vehicle that purchased New Look and acquired a stake of 30.1% each. Founder Tom Singh acquired 23.3% of shares and other management take over 13.4%. Finally these investors took New Look private.	Employees across the ranks were exited about the deal, as they felt this would give the company the opportunity to expand. Employees were directly involved in the transformation process. The equity partners were committed to maintain the previous employment policies. The deal leads to an increase of over 3,500 employees over four years.	World Economic Forum (2008)
Peguform	After the insolvency of the company in October 2002. After Peguform was reorganized the US PE company Cerberus took over the business.	Restructurings at the expense of employees were part of the sale agreements between Cerberus and the company. In the first round 500 jobs were eliminated. A precondition for the sale was a reduction in personnel cost of € 40 million, which represented approx. one sixth of the total personal cost. This reduction was in line with a collective agreement between Peguform and the IG BCE. Increases in working hours to 39 hours per week without an increase in salary and income reductions of 4% were established. Also agreed was a reduction of Christmas and holiday payments. Altogether the burden was 10% per employee.	Van den Burg / Rasmussen (2007)
Picard	In 1994 the company was sold by the French supermarket chain Carrefour. In 2001 Picard was bought by its management and members of the founding family, backed by several French PE company's (MBO/LBO). In 2004 these PE company's exit and sold their stakes to the PE firm BC Partners.	Since the first LBO Picard show a 45% growth rate which had also a clear impact on the development level. In 2002 the company employed 2,200 workers and increased their workforce to 3500 in 2006. Picard invests more than 2.5% of its total payroll in employees training.	Van den Burg / Rasmussen (2007)
Premiere	In 2003 the investor Permira acquired a 64.1% stake in Premiere. In 2005 Premiere went public and Permira obtained 21% of the Premiere shares. In November 2006 Permira exit.	From 2003 to 2004 the workforce was reduced by 10%. Due to restructuring measures Premiere focused on their location in Munich and reduced their capacities at their second main location Hamburg.	Faber (2006)
Stork	The Dutch firm Stork consisted of three divisions: Aerospace, Food and Prints. Until November 2007 Stork the two hedge funds Paulson & Co. and Centaurus owned together 32% of the company's shares. Thereafter the financial investors Candover bought the Stork.	During their investment the two hedge funds tried to split up the company and focus the business on the aerospace section but the management refused such plans. Nevertheless after Candover took over the company, the food section was sold. Following the Dutch labour union they expected job losses due to this split up.	Van den Burg / Rasmussen (2007)

TDC	The former national operator in Denmark was fully privatised in 1998. In December 2005 the Nordic Telephone Company, a conglomerate of five international PE company's (Apax, Blackstone, Permira, KKR and Providence) bought the company for € 11.2 billion. At that time this was the largest LBO deal ever seen in Europe.	Already before the LBO, TDC announced that they plan to reduce their workforce. This plan will be carried on, and it seemed that the new management will speed up this plan.	Van den Burg / Rasmussen (2007)
The Automobile Association (AA)	Formely a member-driven association the company was demutualised in 1999 and sold to the Centrica Group for £ 1.1 billion. In 2004 it was sold on to two European PE funds, CVC and Permira for £ 1.75 billion.	Since the two PE funds bought from Centrica the workforce has been reduced by 3,000 to 7,000. After severe restructurings, job losses totalled 3,000-3,400 out of a workforce of 10,000-11,000.	Van den Burg / Rasmussen (2007)
TUI AG	The company first became a victim of HF in August 2004 when they tried to speculate against the company's share price by short selling. Due to the close co-operation between the management and supervisory boards, a range of defensive measures, and the early publication of positive company results, TUI was able to fight off a major influence of these HF. TUI again came under pressure in summer 2006 when several institutional investors, which held minority stakes, demanded for a company split up into the tourism and the shipping section.	TUI gave in these demands and sold their container shipping section to a consortium in Hamburg. Under the pressure of the financial markets the company has for years implemented cost reduction and restructuring programmes which leads since 2002 to the loss of 6,000 jobs in Germany and further 2,000 worldwide. Nevertheless this actions are not directly connected to a potential influence of the HF.	Van den Burg / Rasmussen (2007)
Unipart	In 1987 the automotive parts producer and distributor Unipart was privatised in a management-employee buy-out that gave private equity firms 56.3% of the equity. Seventy managers obtained 10% of the equity and the general body of employees held 12%. Two years before privatisation it cut 15% of the workforce.	The new owners remodelled the way the company operated, enhancing multi-skilled workers and a direct communication between management and employees. The company changed the system of remuneration so that all workers were paid salaries instead of hourly wages. With the help of a company owned university workers are trained. To be more flexible within this new course the company ended trade-union recognition.	Thornton (2007)
Viterra	Viterra is a residential property company and was owned by the German E.on AG. In August 2005 Viterra was sold to Deutsche Annington, a subsidiary of the British PE company Terra Firm.	Before the deal Viterra employed 1,500 employees, while Deutsche Annington had a workforce of 500 employees. After the acquisition Deutsche Annington planned to dismiss 500 employees. Due to an additional restructuring programme further 400 jobs should be cut.	Van den Burg / Rasmussen (2007)