

RESTRUCTURING IN THE MIDDLE OF ECONOMIC TURMOIL¹

You have recently been promoted to the position of General Manager in a well-known Fast Moving Consumer Good company in Greece, FOC S.A. It's September 16th 2008, Monday morning 8h30, you are in your kitchen reading in the Financial Times the report concerning yesterday's announcement of Lehman Brothers' bankruptcy.

You remain voiceless. You are convinced the Greek economy will not do well in the next following years. It's your second week in your new job; you already realized in your first reviews that the company had too many people in the payroll.

The most unstable post-war economic period is coming, and you are in the middle of the turmoil. You just left a big job in Paris and moved to the sunny Greece, but there is no time to regret the decision.

What do you do? Do you cross your fingers and wait for the big tsunami wave? Do you decide & act?

The first decision you take is to delay "any decision" for a few weeks. This gives you time to analyze carefully the situation. You start thinking about the whole situation and the different possible scenarii.

This is the information you decide to gather:

- 1) Greek economic context
- 2) Company figures: sales, profits and main financial KPI's
- 3) Company organization

In light of this information, what are you going to decide in the middle of this turmoil?

1. GREEK ECONOMIC CONTEXT: 2008

The Greek economy is still growing in 2007 (+4,5% of GDP growth) but showed first signs of deceleration in 2008 (Q1 +0,1% and Q2 +0,1%, see appendix 1).

In the last 5 years economy was growing at strong pace (+4,3% in average). The main reasons behind were:

- An expansive fiscal policy. Public spending was growing at high rate, quicker than GDP growth, which generated big public deficits.

¹ This case has been written by David Cabero, with the collaboration of Marc Le Menestrel, Barcelona School of Management, Universitat Pompeu Fabra, April 2013.

- Easy access to credit and interest rates at record lows. The membership in euro area worked as an umbrella while spreads of Greek debt vs German debt had been kept at historical lows.

For how long would the markets allow Greece to run strong public deficits? If economy slowed down, deficits & debt would reach unsustainable levels.

In 2006, Public Debt overcame the level of 100% of GDP. But still, the markets did not fear the possibility of bankruptcy in the forthcoming future. You knew that applying simple mathematical rules we would be at 120% debt in a few years. And probably, Greece would reach 150% some years later (see appendix 2).

Unhopefully public spending was not used to develop infrastructure and sectors where Greece had competitive advantage (tourism, green energy or qualitative agriculture products). The use of it was inefficient and spent through growing bureaucracy. Public employees were already 1 million weighting for 25% of total occupied population.

Low cost of capital had not generated additional investment in industry and foreign capital was going to emerging markets instead. Easy credit was being used by families to build bigger houses and to finance luxury cars and boats.

Additionally, Greece was losing competitiveness vs its European peers with inflation that scored +3,1% on average during 2004-2008 period, thanks to salary increases and credit expansion.

As for most of small national markets (Greece counts 11 million inhabitants), competition from foreign companies was very limited. The market was too small to attract all international players. This is one of the reasons why competition was reduced in most sectors, prices growing and securing fat margins for international companies operating in Greece.

Consumers were still quite “brand oriented”, with private label representing a small percentage of sales in retail food chains (25%). The fact consumer choices were not so elastic to price changes was also a key factor to explain why inflation was kept so high all these years.

Greek companies were too focused on the internal market, and just a little bit in the closest neighbours, the Balkan countries. The fact they were not exposed to growing emerging markets (Asia & Latin America) was also a disadvantage.

The main conclusion, if crisis came, as one could expect, internal consumption would be strongly impacted; and exports could not compensate the loss. The country would be in free fall.

All these were not really good news.

2. COMPANY FIGURES

FOC S.A. had three business units in its premises in the Northern Area of Athens: the factory and R+D producing for all Group Worldwide subsidiaries and the domestic business. Each business was separated. It was not a chance for you to manage the business that would suffer the most: the domestic business with 150 people out of 1.200 headcount in Greece.

The domestic business was the team in charge of all operations related to two countries: Greece and Cyprus. These teams were selling all company range of products in those countries.

The main figures were:

- net sales 30 M EUR
- EBIT 6 M EUR (20% of net sales).

For each 100 euro of sales, the repartition in the profit & loss accounts was the following:

	In euro
Net Sales	100
Cost of goods	<u>50</u>
Gross margin	50
Freight & distribution	5
Brand support	<u>3</u>
Brand contribution	42
Operating expenses	<u>22</u>
EBIT	20

The company had healthy earnings and a solid Balance sheet without debt. What could happen from now on?

If crisis came, companies exposed to consumption trends would have to face strong declining markets (probably yearly decreases of -10%). In case of long crisis (3-4 years) then the cumulated impact in sales and profits could be strong. Eventually, we would not generate any more profits in Greece.

What could compensate the loss of profits?

- 1) Launch of new categories to generate more sales;
- 2) Cost reduction;
- 3) Doing both at the same time: launching new categories & reducing costs.

You have been building your own personal values throughout your career. And today, as Senior Manager they have a strong influence in your decisions. You just learn that one of the five values of FOC S.A. is "Ethics". This means that restructuring cannot be the FIRST solution in your different scenarii.

3. COMPANY ORGANIZATION

Headcount of FOC S.A. is 150 people.

The details by department:

Sales & marketing	60
Operations (warehouse & customer service)	35
Administration (Finance, IT, HR, General Mangement)	55

Sales are done through internal sales force and exclusive distributors. Internal sales teams cover big cities (Athens, Salonica, Patra, Crete), the rest of the territory is covered through exclusive distributors. The two biggest cities (Athens & Salonica) weight for more than 50% of the total population of the country.

You plan interviews early October with the responsible of each department to analyze thoroughly the situation.

You ask some KPI's (Key Performance Indicators) to Headquarters and you learn that all other business subsidiaries in Europe had less than 100 people, with the exception of France, which was doing 4 times de sales of Greece with less than 120 people.

At a first glance it seems the company could properly work with around 100-110 people, or even less. Selling 200 thousand euro per worker is low by all FOC S.A. standards.

The domestic business you lead has also a factory producing pantyhose, the only one in the group since Greece is the only country selling this line of products. The payroll in the factory is 80 people, producing 5 million pairs a year.

At that time, main worldwide producers of pantyhose are Italian and are based in a small Italian town close to Milano. You decided to go there in a two day trip. Your main conclusions are:

- Big players are producing 70 million pairs a year
- Economies of scale in the factories & purchasing power are keys to get low production costs. Italian costs are around 40% to 45% lower than ours
- Chinese would probably be the next, producing at even lower costs
- One day we would be competing with Italian and Chinese private label products in the shelves of Greek retailers

Whatever the decision is, we should have “competitive” pricing in the stores.

4. DECISIONS TO TAKE

The decision making process started.

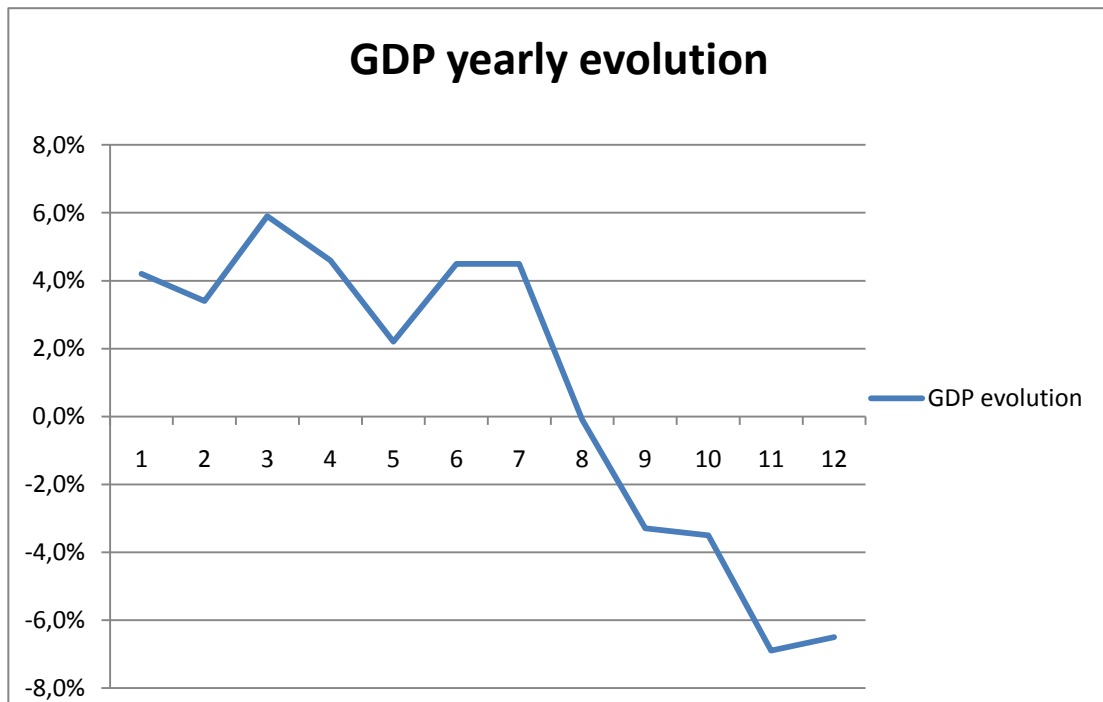
- 1) Since you believe that sales would decrease in the next following years, should you:
 - a. start looking for other product categories to boost sales (which ones)
 - b. start reducing headcount (which departments)
 - c. find external customers in pantyhose category to increase factory output and productivity which would allow you to keep the factory while keeping competitive costs
 - d. close the factory down
- 2) Once you take your decision:
 - a. what would be the next steps.
 - b. What and how you communicate?
 - c. To whom?

*Alea jacta est*², you are now deciding in the middle of economic turmoil. What is your decision?

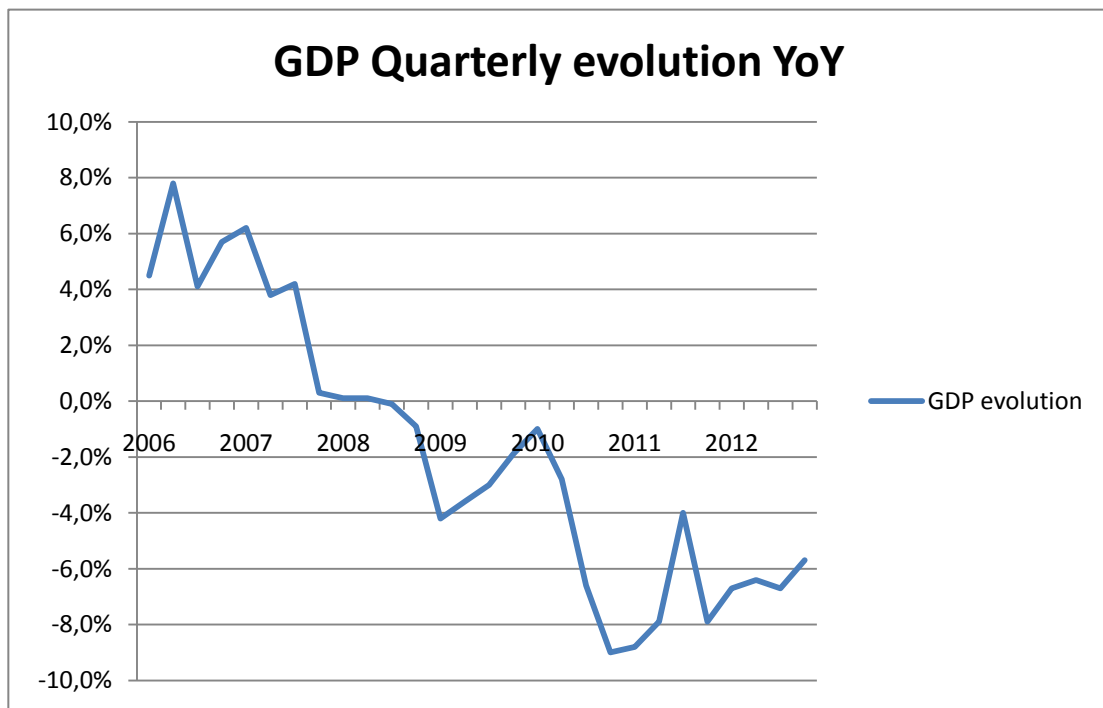
² Like Ceaser thought before going through the Rubicon River (between Italy and Galia Cisalpina).

APPENDIX 1:

Even if deceleration started at the end of 2007, the first negative figures came after Lemman Brothers collapse at the end of 2008.



Source: National Greek Statistics Bureau (Elstat)

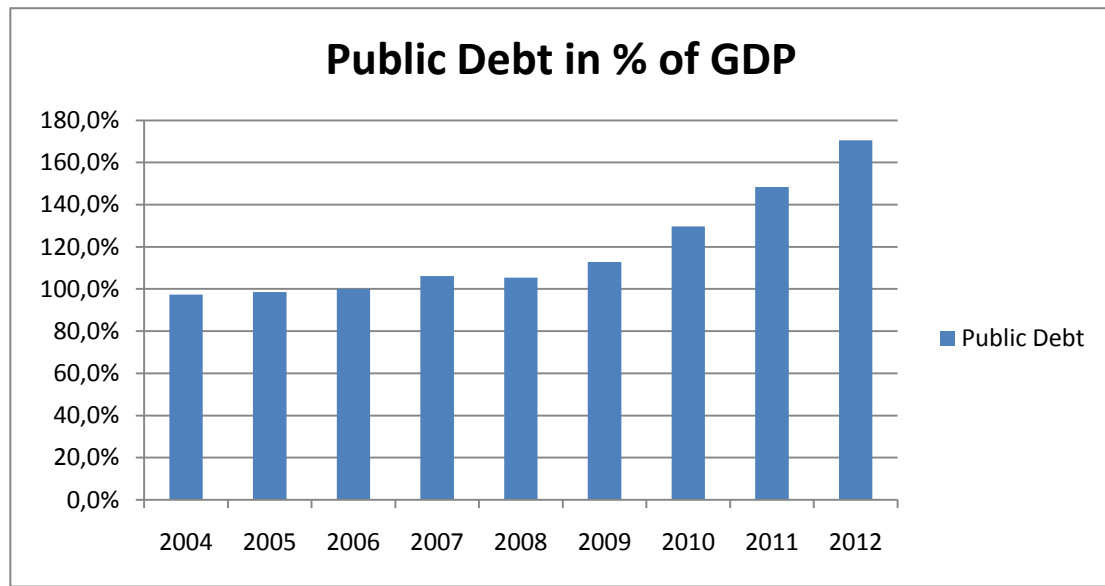


Source: National Greek Statistics Bureau (Elstat)

After 18 consecutive quarters of GDP decrease, GDP in the 4th Quarter of 2012 was -23% lower than the one in 2007.

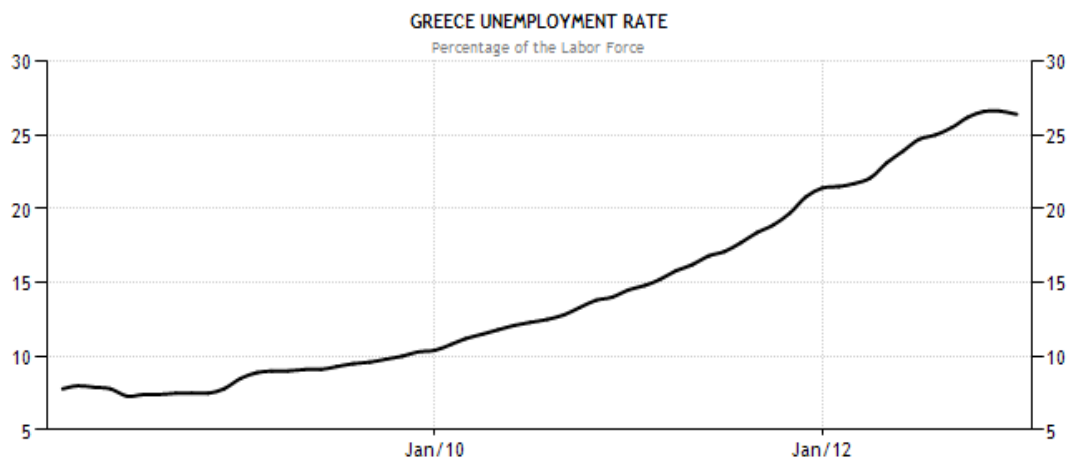
APPENDIX 2:

Public debt increased in 4 years from 105% to 170% of GDP due to strong public deficits & deep recessions.



Source: <http://www.tradingeconomics.com/greece/government-debt-to-gdp>

APPENDIX 3:



SOURCE: WWW.TRADINGECONOMICS.COM | HELLENIC STATISTICAL AUTHORITY

APPENDIX 4: Thoughts Around Decision Taking

Basic types of decisions:

Strategic decisions: Managers have weeks or months to make these decisions, which have life-shaping effects on a corporate or personal level. Strategic decisions are very important, involve significant uncertainty and complexity, and are hard to think through.

Typical decisions: These decisions often come from team meetings that last a few hours. They can have a big impact, but they are frequently tactical in nature and arrived at through a collaborative process.

In-the-moment decisions: For decisions made on the fly, managers use a different part of the brain that emphasizes rapid pattern recognition. Beginning with limited or incomplete information, they habitually look for similarities to experiences they've had in the past.

What is a “good” decision?

Six elements to generate a good decision making process:

- (1) The right frame: making sure you're solving the right problem in the first place; to start with the “right” question.
- (2) Clarity about what you want. For example, are you trying to maximize shareholder value or just trying to stay alive and minimize damage?
- (3) To think about creative alternatives.
- (4) To Gather the right information, including information about uncertainty, which is essential if you want to choose the best alternative.
- (5) Reasoning, which includes what you know and what you don't.
- (6) A commitment to make it happen, since a decision is no stronger than its weakest link.