



Seeing the light

The restructuring of German-owned vehicle mirror and lighting business Schefenacker was a complex undertaking, involving a relocation of the group's holding company to the UK. *Restore* investigates...

In the spring of 2007, the English coastal village of Portchester welcomed a new corporate citizen. Schefenacker, a manufacturer of mirrors and lights for the global automotive industry, relocated its headquarters from the German town of Schwaikheim near Stuttgart to Hampshire in the UK as part of a wide-ranging restructuring operation. It was a move that enabled a troubled company to ward off the current constraints of German corporate law and the German Insolvency Code, while implementing a rescue plan that would satisfy the demands of its financial backers. That the strategy succeeded was good news not only for Schefenacker itself, but also for its car-industry customers.

The survival of Schefenacker was, in the short term at least, hugely important to the industry. The world's vehicle manufacturers tend to rely on a relatively small number of component suppliers and there isn't a great deal of slack in the system. If a key player runs into difficulties or goes out of business, it could be weeks or even months before its customers can source vital components elsewhere.

Schefenacker is certainly a key player. The company supplies most of the

world's major car manufacturers with mirrors and has a market share of around 28 percent. As Samantha Bewick, Director at KPMG in the UK and joint CVA Supervisor during the Schefenacker restructuring operation, points out, the realities of 'just-in-time' supply chain practices mean that competitors are simply not producing the volumes that would allow them to step in quickly and replace Schefenacker's contribution. "Had the company gone out of business, production lines would have ground to a halt," she says.

Trouble starts

Despite having such a large share of the rear view mirror market, by 2006, Schefenacker was experiencing severe financial difficulties. To some extent, the company was feeling pressures that weighed on the whole industry. The last few years have been difficult for the world's car manufacturers, and, to stay competitive, many have been controlling costs by demanding lower prices from their suppliers. Like most of its counterparts in the sector, Schefenacker was feeling the heat.

The company also had its own internal problems. In addition to its cash-generative mirror business, the



Picture: Getty images

company also supplied lighting to luxury marquees, a business area that needed major investment in research and development. "It was burning cash," says Bewick.

In fact, it was set to run out of money in the short term, and even with mirror manufacturing making a profit, the group as a whole was not looking at a sustainable future. What's more, the company had expanded internationally, building up considerable debts, which

Andersch, Restructuring Partner at KPMG in Germany. "Lack of liquidity (or inability to pay) is the most common reason to open insolvency proceedings in the German automotive sector."

With the clock ticking, the company and its advisors began working on a route map for rapid recovery. Or to be more precise, an interlinked series of routes. To turn the company around, it was necessary not only to renegotiate trading terms with

Legal issues

In terms of German company law, it was a proposed debt to equity conversion that posed the thorniest problem. Mark Sterling, Managing Partner at law firm Allen & Overy, acted as corporate counsel for Schefenacker during the complex restructuring process. As he recalls: "It was by no means clear if a debt to equity conversion of a German company could be successfully implemented under German law."

So, a decision was made to move the headquarters of Schefenacker to England and seek a Company Voluntary Arrangement (CVA) under UK insolvency law. One advantage of this approach was that, in England, the claims of Schefenacker's creditors and stakeholders could be heard and addressed under a single process. In Germany, there would have been a number of parallel proceedings.

The first task was to convince the various stakeholders that a transfer to the UK was in everyone's interests. Once this had been done, Sterling and his legal team had to ensure that the transfer of the holding company from Germany to Britain would comply with the legal requirements of both



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Mark Sterling, Managing Partner, Allen and Overy

by 2006, it was not in a position to service. It was clear that restructuring was required.

The nettle had to be grasped quickly, not least because German company law imposes a strict timetable. "In Germany, if directors believe that a company is insolvent they have to file proceedings immediately unless the situation can be resolved within 21 days," says Tammo

its customers, but also separate the loss-making lighting business from the profitable mirrors business, whilst restructuring the group's balance sheet and reducing its debts through a debt to equity conversion.

These four elements of the package were interconditional and all needed the consent and support of stakeholders.

jurisdictions. It was a painstaking process. Schefenacker was configured as a German Limited Liability Partnership. Moving to the UK involved transferring ownership of the business to a general partner that would be recognised by the British courts.

Achieving consensus

Once the relocation was complete, the next step was to get a consensus on how the company's debts could be restructured. "We were dealing with many stakeholders," says Sterling. "Each had their own leverage and were seeking to protect their own interests."

At the top of the debt chain were the suppliers of revolving credit facilities. They had the right to be bought out by other lenders, and their main objective was to either realise the value of their debt or be bought out at par. Then there were the second lien secured lenders. Failure to agree a deal would see those lenders taking steps to enforce their security. The third group was made up of institutional and retail bondholders, which were in an interesting position.



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Samantha Bewick,

Director, KPMG in the UK

While they were out of the money, they were in a position to vote down any deal agreed by the other stakeholders. Finally, there was the company's owner, Dr Alfred Schefenacker, who wanted to retain a significant stake. The challenge was to get this disparate group to agree on a restructuring formula.

The restructuring team had one thing in its favour: failure to secure a deal would result in everyone losing out. Even so, securing cross-the-board agreement was never going to be easy. Unusually, the majority of the bondholders were retail investors. Although they did not play a direct



Picture: Corbis Images

role in the negotiations, they would have been acutely aware that their personal wealth was at stake. What's more, many of the bondholders also felt a personal attachment to the business itself. "These were German bondholders and they regarded Schefenacker as a German company. There was a lot of emotion and concern about its future." As such, they could not be expected to simply rubber stamp any deal agreed by the other stakeholders.

Indeed, when the other stakeholders emerged from negotiations with a restructuring formula agreed, it quickly became apparent that the proposal was unlikely to secure the support of sufficient numbers of bondholders. Under English law, a 'yes' vote representing at least 75 percent of bondholders was required to approve the CVA. The initial response of bondholders to the suggestion that they would get just 5 percent of the equity was, to say the least, cool. "The first proposal wasn't particularly generous to the bondholders," says Sterling. "The company therefore suggested a more generous proposal that had a greater chance of success."

That second proposal offered bondholders 7.5 million euro in cash, plus 5 percent of the company's shares and an option to subscribe at a nominal price for 10 percent more, conditional on certain targets being achieved. As part of the same deal, the secured lenders would get 69.6 percent of Schefenacker while also providing more cash and reducing the company's interest payments. Dr Schefenacker would buy a 25.4 percent stake, effectively putting 20 million euro into a new mezzanine finance facility, and

write off around 100 million euro in debt. A new revolving credit facility of 2.5 million euro was put in place.

Turnaround complete

The restructuring still hung in the balance. The vote was postponed to allow Schefenacker and its advisors time to communicate with the bondholders and win hearts and minds. There were still rumblings of discontent, but when the poll finally took place, the proportion in favour exceeded the required 75 percent. The margin was narrow, but a debt-equity conversion had been achieved. However, the financial restructuring alone would not have been sufficient to secure the long-term future of the company, so it was also agreed that the lighting division should be sold for a nominal one euro. On the operational side, the company agreed new supply terms with its customers and a fresh management team was installed. A full refinancing was also achieved to provide appropriate medium-term facilities.

Schefenacker now has the financial resources to continue trading, while the value of its debt repayments has been more than halved. "It has a platform from which it can continue as a powerful player in the automotive industry," says Mark Sterling. **R**

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