

## **THE LONG TERM IMPACT OF DIFFERENT METHODS OF BOOSTING THE ACTIVITY**

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**Abstract:** *The activity of a company, given the actual conditions characterized by financial difficulties due to the economic crisis, are confronting a conglomerate formed by difficulties and unknown elements whose management involves the detailed knowledge and understanding of the phenomena that gravitates in the activity area of the company. The economic crisis that has challenged the survival of the companies transmitted to the management that in order to survive certain environment troubles, it is necessary for the companies to be flexible, the measures to be adopted rapidly and the companies' objectives to always target the insurance of profitability and necessary cash flow. The non-fulfillment of the objectives that target the profitability and insurance of cash flow leads to a company in difficulty. A company that is not profitable cannot continue its activity because the funds at its disposal do not allow normal financing of the operating cycle. The fact that the Romanian economy has gone through a hard and unknown path, from an economy that worked under planned economy principles to a market economy, is remarkable. The fact that companies went through different extreme situation needed recovery strategies and revitalization of the activity in order for them to resist and overcome the difficult moment. The privatization, merger/acquisition, insolvency do not mean a recovery and revitalization strategy, but only a method. In this regard, a strategy may include more methods that can be applied in*

*different stages of the evolution of a company. Regarding the results a method or a recovery and revitalization strategy may have, they depend very much on the external environment of the company and the management's ability to take into consideration all the variables that may influence the results. Only by referring to the privatization process that took place in Romania and the diversity of methods through which it was made, we can conclude that its quantitative dimension will not be found in a near future. In the same conditions we can also discuss about the volume of nationalizations that were made at the middle of the XX century.*

**JEL classification:** M16, M42, M49

**Key words:** privatization, insolvency, difficulty, fusion, division, evolution.

## **Introduction**

Choosing the general strategy and the methods of revitalizing the activity (internal growth, acquisitions, divisions, fusions, etc.) is based on the characteristics and stability of the company and a very good understanding of the external environment. Another important aspect in choosing the methods that compose a growth strategy is represented by the assumed risk that depends both on the internal situation and the competitors' situation. It is necessary that any long term growth strategy include more methods, both of internal growth and also the possibility to make acquisitions and fusions on the targeted markets or to resort to financing in order to develop the capacity. An important aspect in successfully applying the strategy is the familiarization of the management with such operations and its ability to manage them, given that the competition is fierce and the market does not allow waiting moments or errors of implementation. Given that not even the definition of what it is supposed to be the application of a growth and revitalization of an activity strategy is not a simple and clearly defined initiative it is obvious that implementing it in practice is not an easy task.

## **Analyses**

The activity of a company, in current conditions, is confronted with a conglomerate formed by difficulties and unknown elements whose management involves the detailed knowledge and understanding of the phenomena that gravitates in the activity area of the company. The economic crisis that has challenged the survival of the companies

transmitted to the management that in order to survive certain environment troubles, it is necessary for the companies to be flexible, the measures to be adopted rapidly and the companies' objectives to always target the insurance of profitability and necessary cash flow. The non-fulfillment of the objectives that target the profitability and insurance of cash flow leads to a company in difficulty. A company that is not profitable cannot continue its activity because the funds at its disposal do not allow normal financing of the operating cycle.

In order to actually analyze the long term impact of different methods for the revitalization of the activity, we analyzed the first 100 companies<sup>4</sup> (from the manufacturing industry) based on the turnover form 1994 (equivalent in mil dollars), that can be grouped in 4 categories:

- 11 companies have the turnover equal to 0 due to fusion operations through which they passed in the current period (dissolution without liquidation);
- 22 companies adopted strategies for the revitalization of the activity that led to higher turnovers in 2013 than the ones made in 1994;;
- 31 companies, following the adopted strategies, registered smaller turnover in 2013 compared to the one in 1994;
- 36 companies have the turnover 0 or are dissolved through liquidation.

An example of similar companies that had completely different destinies due to the management's decisions is represented by Arpechim S.A. and Petrobrazi S.A.. In 1994, Arpechim has registered a turnover (updated) of 435 mil dollars and Petrobrazi 423 mil dollars. For the year 2013, the results have been completely different, given the fact they are managed by the same management. Petrobrazi has been the subject of a merger in 1997 (dissolution without liquidation) being included in Petrom and subsequently being privatized in package toward OMV. At the moment it is the only raw material refining unit from Petrom-OMV in Romania. It benefits from a special attention from the Petrom-OMV management, periodically being the subject of important investments for modernizing the refinery capacity. Arpechim had the same track as Petrobrazi, only after one year. At the moment any activity is stopped and the company is the object of several negotiations between the Romanian State and OMV on one side and the Romanian State and foreign investors interested in the privatization of OLTCHIM on the other side. Another sensible subject of these negotiations is represented by the environment obligations, not-honored at

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<sup>4</sup> The estimation tied to the turnover from 1994 and 2013 belong to the Financial Journal publication based from information from the Trade Register and the Ministry of Finance, "How the top 100 companies from 1994 look today. Half of the Romanian industry disappeared"; 14<sup>th</sup> of September 2014.

the moment by OMV that rise up to 250 mil EUR (for this industrial objective).

Oltchim was one of the largest chemical product companies in Romania and South-East Europe and represents the last functional entity from the petrochemical domain in Romania. The company is linked to the Arpechim Pitesti refinery through underground pipes of ethylene and propylene, from which it obtains the raw materials necessary for the production activity. Currently the Romanian State holds a majority participation, but insufficient in order to adopt/approve certain measures so that to facilitate the privatization. Oltchim has been through different privatization processes, but each time they failed, because the lack of activity of the Arpechim refinery lead to the impossibility to insure the raw material and thus to a low productivity. Another difficulty is represented by the debts the plant has, that cannot be converted in shares due to the denial of the minority shareholders who feel their participation is threatened. Currently, Oltchim is in state of insolvency, but working, operation results are positive and negotiations are being held, on one side with Petrom-OMV to take over the Arpechim refinery and on the other side with possible investors that might sustain the plant.

The Rafo company has been privatized in 2001 by selling a 60% share package to a corporation formed by Imperial Oil and Canyon Servicos. The value of the transaction was of 7,48 mil dollars. In the first half of 2004, the company started proceedings insolvency due to the financial difficulties and debts toward the state budget. As a solution to the company's situation, at the end of 2004, Rafo debts toward the state budget were converted into shares. The Russian businessman Yakov Goldovsky, acquired through different companies the majority share package and started an important recovery program. In 2007, Rafo paid the debts toward the state budget (approximately 898 mil Ron), acquired Darmanesti refinery and benefited from a share capital increase in order to rebalance the financial necessities of the company. At the beginning of 2015, the company's majority shareholder (Petrochemical Holding – controlled by Yakov Goldovsky) approved the shutdown of the refinery and selling it for scrap.

In 1999, the Dacia plants have been privatized by selling a 51% package toward the Renault car manufacturer. The latter is obliged to pay 50 de mil dollars to the Romanian State and make investments in value of 220 mil dollars. The Renault Group continued to acquire the other shares of the Dacia plant, thus currently holds 99,14% of shares which permitted it to delist the company. Renault is a French company that was also privatized in the period 1996 - 1999. The strategy for the Dacia plant for created on long term, the company obtaining profit for the first time after the privatization in

2006 and at the moment is one of the most important companies in Romania that has developed the economic environment both vertically and horizontally.

Tractorul UTB S.A. had in 1990 approximately 23.000 employees and followed a privatization process in order to be upgraded following the need to enter on new markets (compared to the traditional ones). This long privatization process often attracted the employees' dissatisfaction that were afraid of the potential investors' intentions and entered on strike or made street protests to attract public attention. As recovery measure, the company turned to a division in 6 companies in the year 1999, thus the following companies being created: Prorem UTB, Frimut UTB, Rentcom UTB, Scudiver UTB, AWE-HD, MUM-UTB. These companies went in the property of several Romanian businessmen, but that did not have the investment power or the know-how necessary for the recovery of the activity. In 2004, the Italian company ARGO, the manufacturer of the Landini tractors, wished to buy the plant but due to the administrative instability at local and central levels, the privatization stopped. In 2005, the company Mahindra showed interest to take over the plant, but the intention did not materialized. In 2007, the company was put into liquidation and the assets were bought by an investment fund that carries out activities in the real estate domain, currently a mall being built.

Given that the number of the acquisition transactions in Romania, made in 2014, was smaller than the one in 2013, their value reached the maximum of the analyzed period, being with 100% bigger than the following value as size (reached in 2012). This situation is due not only as a result of 2 years of national economy growth (approximately 3% annually), but especially due to the prognosis for the period 2015-2020. Given that an investor, in his medium term strategy, includes achieving value procurement (which emerges from a 200% increase in Top 10 value transactions in 2014 to 2013<sup>5</sup>), it also analyzes the stability and growth potential of the market in a higher extent than the results obtained in the past.

The results reached in Romania's case are due to the fact that a number of cross border companies have upgraded their activity also in other countries and acquired companies from Romania that overtook the production/activity volume. This situation led to a migration of the labor work on all levels of professional specializations.

If we make a comparison between the acquisition and merger evolutions between Bulgaria, The Czech Republic, Poland, Romania and Hungary and the GDP evolution per capita, the situation is as follows:

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<sup>5</sup>„Emerging Europe: M&A Report 14/15”, Euromoney Institutional Investors Company (EMIS) and American International Group (AIG), 2015

		2011	2012	2013	2014
Bulgaria	Number of transactions	120	83	73	69
	Transaction value	1204	1240	1489	1067
	GDP per capita	5100	5200	5200	5400
	Top 10 transactions value		402	1333	802
Czech Republic	Number of transactions	153	102	153	171
	Transaction value	1556	1297	5709	5018
	GDP per capita	15200	15000	15000	15200
	Top 10 transactions value		589	4971	3457
Poland	Number of transactions	516	331	363	285
	Transaction value	18000	9000	11600	4500
	GDP per capita	9800	10000	10100	10500
	Top 10 transactions value		4619	6248	2123
Romania	Number of transactions	162	118	150	132
	Transaction value	1264	1464	1185	2941
	GDP per capita	6400	6400	6700	6900
	Top 10 transactions value		465	714	2139
Hungary	Number of transactions	137	102	102	134
	Transaction value	3933	729	1520	773
	GDP per capita	10000	9900	10100	10500
	Top 10 transactions value		372	1166	403
Total	Number of transactions	1088	736	841	791
	Transaction value	25957	13730	21503	14299
	Top 10 transactions value	0	6447	14432	8924

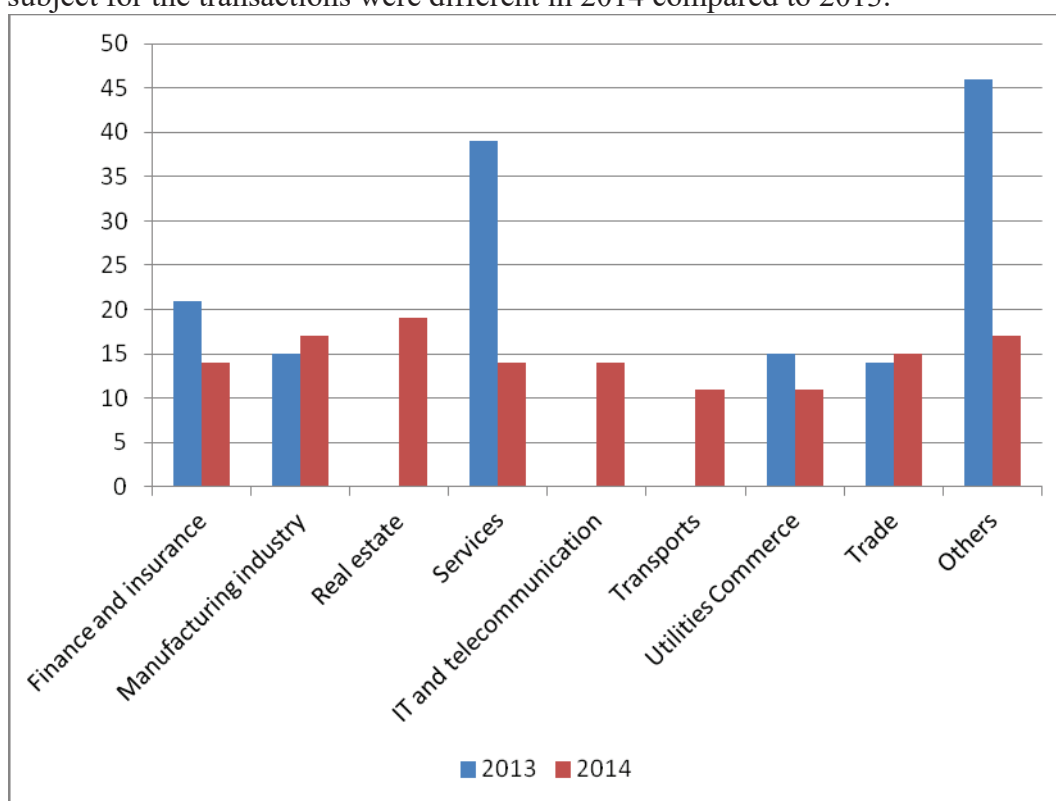
Source: DealWatch, EMIS, AIG; EUROSTAT

Table no. 1: The number of transactions' evolution, total value of transactions/top 10, GDP per capita

The total of the transactions made in the mentioned countries register a decrease of 297 transactions. In 2012, compared to 2011, the decrease is of 352 de units and is generated by the decrease of the number of transactions in all the analyzed states, which generated a decrease of 12,227 billion EUR of the transactions' value. From a macroeconomic evolution point of view, the only states that registered improvements of the GDP per capita indicator were Bulgaria and Poland. The year 2014 represented another year of decay for merger and acquisition market compared to 2013, both in means of number of transactions (791 in 2014 compared to 841 in 2013), as also value (14.299 mil EUR in 2014 compared to 21.503 mil EUR in 2013), given that the GDP per capita indicator registered substantial appreciations in all the mentioned states. The situation can be explained by the economic and political difficulties that Russia has

confronted in 2014 (a main investor in the mentioned markets) that led to the dilution of demand in this market and automatically both of the transactions and its values. From the point of view of the evolution of the value of the 10 most important companies from the mentioned states, it cannot be generally characterized because it contains unique and subjective manifestation elements and the evolution does not take in consideration quantitative indicators (macroeconomic evolution, merger and acquisition market evolution), but qualitative indicators that refer to the company that was the transaction's object and the moment it has been made.

Given the fact Romania is receiving positive feedbacks from the investors as a result of investments in infrastructure, it is mandatory for the development strategy for the next period to target the utility of both national and European funds for strategic investments that will continue to attract investments in the private sector and a growth superior to the actual rate with the purpose to reduce the gap with the western economies. According to the graphic, it can be seen that the investors trust the Romanian economy in general, because the sectors in which activate the companies that were subject for the transactions were different in 2014 compared to 2013.



Source: Emerging Europe: M&A Report 14/15", Euromoney Institutional Investors Company (EMIS) and American International Group (AIG)

Graphic no. 1: Distribution on sectors of the number of mergers and acquisitions

It is essential for the business environment and for the potential investors, that at a national level, there is stability regarding the regulations of different domains, and here the reference is the annulment of the beginning of the investments and selling at an undervalued price the parks that produce green energy, but also strictly respecting the investment and privatization calendars. In Romania the agriculture is underdeveloped and can attract important investments if the Romanian State will support this domain through the necessary infrastructure and transparent financing of projects through the National Rural Development Program. Another aspect to be highlighted is linked to the IPOs that recently took place, that were almost totally and stirred the investors' interest in the energy domain.

Regarding the transactions' value and their percentage in the total of issued transactions, the idea exposed previously is highlighted, that the Romanian economy shows interest and the number of transactions and the value they are made at are influenced only by finalizing the negotiations and procedures, regardless of the activity's domain.

A subject to follow in the future years is linked to the evolution of the relations with China that in a first stage opened a credit line of 10 billion dollars for investments in Romania. These investments are wished to represent examples of good practice in a development strategy of investment and commercial relations with Central and Eastern Europe. The last evolutions on China's stock exchange market from the summer of 2015 may lead to the renouncement of the desired expansion in order to stabilize the internal market, severely affected by the decrease of the stock indicators.

## **Conclusions**

As recovery and revitalization method, as long as the strategy is adopted until the company enters in a difficulty situation; commercial companies can turn to obtaining non-refundable grants. The investment projects to raise competitiveness, (partially, based on state aid schemes) financed by the European Union, cover a large activity domain pallet and usually assume increase of the production ability that can generate positive results. The obtained results (their forecasts) must not have a profitability rate too big as they can be achieved through bank credits to be paid with the plus value created. Taken all this is consideration, it is necessary for the investment project to be accordingly to the growth and revitalization strategy, to efficiently use the current information and to plan the development ability of the company.

One of the mechanisms the state has at hand, with the purpose to revitalize the companies' activity is represented by "The Increase of the Economic Competitiveness" Sectorial Operational Program and has as



objective the improvement of the Romanian companies' productivity with the purpose to reduce the gaps compared to the European Union's level. SMIS is a centralized information system with the purpose to monitor the projects from the submission of the application to the finalization of the sustainability period. In this program it is being registered all the information linked to a project and obtaining the assumed results. Within the "Primarily Axis 1 – Innovative and eco-efficient production system; Major Intervention Domain DM1.1 – Productive investments and training of companies for the competition in the market, especially the SMEs", the assumed results were referring to the number of the new created jobs, the number of the kept jobs, the number of tangible and intangible acquired assets and the increase of the turnover. Within the Major Intervention Domain1.1, in SMIS there are (July 2015) 227 de beneficiaries for whom the progress reports are being introduced with information linked to the evolution of the turnover, according to the next table:

Turnover evolution	Number of companies
negative	4
0 <turnover> 25%	91
25% <turnover> 50%	32
50% <turnover> 75%	32
75% <turnover> 100%	17
100%<turnover	51

Source: SMIS

Table no. 2: The increase of the turnover following the appeal to non-refundable grants

According to the data presented in the previous table, 40% of the applicants registered increases of the turnover up to 25% as a result of implementing the project. Of the analyzed companies, 4 beneficiaries of the non-refundable grants confronted with difficulties and register smaller turnover that in the moment of submitting the application, existing the risk for the provided help to be recovered due to the un-fulfillment of the indicator. Of the applicants that registered growths of the turnover higher than 100%, 8 applicants are situated in the interval 400% - 1049%, and other 16 in the interval 200% - 399%. In the component of the 227 companies, there are 152 small companies and 75 medium companies. Analyzing the previous presented data, we can conclude that turning to non-refundable grants may represent a revitalization instrument due to the fact that 98% of the companies whose progress reports were introduced in the SMIS, registered increases of the turnover.

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