

Gongwer News Service: Private Equity could Impact Michigan

NEWSMAKER FRIDAY: PRIVATE EQUITY BUYOUTS COULD AFFECT STATE

When it was announced last week that Daimler would sell 80 percent of its ownership of Chrysler to private equity firm Cerberus Capital Management, it was a big deal for not just the auto industry, but also because it signified one of the most high profile buyouts of public companies by private equity firms, many of which are happening in Michigan.

Although the amount of private equity firms and hedge funds purchasing public companies has increased and garnered attention in the past several years, few people are sure what the exact impact of buyouts will be. Whilesome say they can turn distressed companies around, others worry about the impact they'll have on workers.

Many say if private equity firms invest money and turn the companies around, the purchases can help the state's economy by making these companies profitable. If they decide to divide the company up and sell it off to make a profit, it can be harmful, they also say.

The buyouts are occurring in all kinds of industries from electronics to automobiles to automobile parts suppliers, and many of those deals are happening in Michigan.

Besides Cerberus Capital Management's \$7.4 billion purchase of Chrysler, other private equity firms, like soon-to-be public equity Blackstone Group LP, also expressed interest in Chrysler.

Private equity firm Platinum Equity Holdings LLC proposed to buy part of Troy-based Delphi Corp in January, and investor Carl Ichan has offered to buy Southfield-based Lear Corporation. The Carlyle Group, along with several other groups, bought the Hertz Corporation.

The companies that are being bought up by private equity firms are ones in transition or having financial difficulties, said Jim McTevia, a managing member of McTevia and Associates, and they're found in all kinds of fields and endeavors.

He's spent 40 years working as an advisor with companies in transition and said private equity firms buy companies with money from investors and purchase companies they know will be successful with globalization, are ready to expand into global markets and can make money. The potential to make a payoff makes them anxious to buy companies in trouble like Chrysler, he said.

"They specialize in buying under performing companies and investing in them, fixing them and making them work," Mr. McTevia said.

Chrysler's future lies in global expansion and global profits and the people who are going to buy Chrysler's cars will be in North America but also in China, Mr. McTevia said, and private equity firms will take advantage of that. If Chrysler can be fixed and turned around it will be a big payday for Cerberus.

Scott Watkins, a consultant at Anderson Economic Group, said the purchase of Chrysler by a private equity firm is a new direction for the automobile industry and is necessary step toward progress, he said.

"The current state of the industry is not working in terms of employee agreements and Ford, Chrysler and General Motors aren't keeping up with global competition," Mr. Watkins said. "It seems clear that any new direction is worth a shot at this point."

Mr. Watkins said even if the purchases don't turn the companies around, their actions would send a message.

"If nothing else, it shows big labor and the UAW that the OEMs - Ford, Chrysler and GM - are serious about change and that the old negotiations and the old style of doing things is out the window," Mr. Watkins said.

Chuck Hadden, vice president of government affairs for the Michigan Manufacturers Association, said the buyouts by private equity firms is just a different process than what's normally done, not better or worse. The buyouts started with smaller companies and he's seen the number of companies being bought by private equity firms increase over the past few years.

"On one hand, once they've gone private they don't have a lot of the reporting requirements public companies have," Mr. Hadden said. "But if it's the only way the company's going to survive, then it's good."

Companies that are bought by private equity firms can escape the oversight of the federal Sarbanes-Oxley Act of 2002, which established new requirements and rules for public companies. Being bought by a private equity firm can also allow a company to restructure itself outside of the need to report to Wall Street, said Tim Yost, spokesperson for AlixPartners, a global restructuring, consulting and financial advisory firm.

"That can allow a company a more longer term focus," Mr. Yost said.

Mr. McTevia said the benefit to Chrysler from being bought by a private equity firm is that the firm can offer the company the time it needs to create a product consumers are going to buy and expand.

Cerberus can also offer the necessary investment of money Chrysler needs for the future, he said.

"Chrysler's got a good future if Cerberus is willing to spend the money and take the time," Mr. McTevia said. "You can't solve its problems immediately, you've got to reach into the future and Daimler was no longer interested in paying the money to buy time, Cerebus seems willing to pay the money to buy the time."

There has been concern about the impact private equity firms buying these companies will have on employees. The firms want to make money and there's concern the workers could be affected by cost cutting measures.

Mr. McTevia said in many cases private equity firms are going to look at areas where things might need to be changed or restructured. Jobs might be lost or employees transferred in some cases, he said.

"The downside for workers is that the possibility exists where families may have to be relocated or uprooted," Mr. McTevia said. "I don't think there's going to be a major impact on the employee."

The United Automobile Workers has said it supports Cerebus' buyout of Chrysler, with UAW president Ron Gettelfinger saying in a statement that union leaders had consistently said they wanted Chrysler to remain with Daimler but were comfortable enough with the deal to support it.

"There will be an infusion of cash put into this company, and a lot of things are going to happen that are in the best interests of moving forward," Gettelfinger said. "We have to believe they are very concerned about the future of the U.S. auto industry."

Mark Gaffney, president of the Michigan AFL-CIO, said if employees are members of a union they're in better shape in a buyout situation. If a private equity firm decides to keep a company and invest in it the workers will usually be in a good situation, but if the firm decides they can make more money by selling parts of the company off, workers can be at risk, he said.

"All these equity firms buy companies in order to make company, if they can make money by making changes and improving it they will," Mr. Gaffney said. "But if they can make more money by dividing it and selling it off, they'll do that."

If the Chrysler buyout can help increase the company's profitability that could be good for the state's economy, he said.

"These kind of deals can benefit the state if people that run the equity firm are buying the company to run them better or offer new products," Mr. Gaffney said.

In the end, whether a private equity firm buyout will help or hurt the employees will be determined on a case-by-case basis.

"We'll work with them if they become the owners of our companies," Mr. Gaffney said. "We want profitable companies too."

Mike Shore, spokesperson for the Michigan Economic Development Corporation, said whether the buyouts will be beneficial to the state would be judged on a case-by-case basis. What happens will depend on a number of factors unique to each case, he said.

"Our hope and what we work to do in any of these circumstances is keep these assets operating in Michigan and keep jobs at these facilities," Mr. Shore said.

The MEDC generally knows what companies are interested in or involved in sales and mergers and tries to work with them to keep jobs in the state, Mr. Shore said.

Overall the feeling from many is that private equity firms are going to continue to buy companies in the hopes of turning them around for a profit. What that will do to them, or the state, is unknown, most say.

"I don't think anybody knows exactly how it will work and whether it will be good or bad," Mr. Hadden said.

Mr. McTevia said private equity firms are going to continue to pursue companies that are in the global marketplace and will continue to do so as long as they can make money.

"Every day you see private equity firms or hedge funds investing in manufacturers of everything from vacuum cleaners to cars," Mr. McTevia said. "Any company that's got a global presence is going to look very interesting."