

# German medium-sized businesses during the Corona crisis



**Shaping the image of the future in uncertain times –  
M & A as a strategic course of action**

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For the first time in 10 years the German economy is experiencing an unfamiliar situation: it is facing existential problems across the board. After years of growth during which the future outlook was time and again dimmed by global uncertainties such as trade wars, BREXIT, the political situation in the Middle East as well as increasing political and economic interventions, the global corona crisis carries a previously unknown dimension and calls the entire existing economic system into question. The coronavirus and the dramatic economic and financial crash caused by it result in a standstill and uncertainty.

German medium-sized businesses are a dominant factor within the German economy. More than 90 % of the businesses are medium-sized companies, among them many family-owned businesses and „hidden champions“, global market leaders in their field. No other country in the world lists as many market leaders as Germany. In the German economy medium-sized businesses provide almost every other job and every day contribute to the best brand that Germany has to offer: „Made in Germany“.

The initial signals are alarming. In many countries production has ground to a halt, global supply chains have been interrupted, entire industries (e.g. the automotive industry) are staring into the abyss. In the United States unemployment figures jumped to historic all-time highs. The economic collapse of Italy and Spain threatens to reignite the EURO-crisis. Despite all the interventions by the central banks, the stock markets are experiencing great turbulences.

## After the crisis will not be before the crisis

Without wanting to exaggerate or being overly pessimistic, it is an educated guess that after the crisis will not be before the crisis. Nobody knows how severe the shake-up of the corona crisis will be. Moreover, this uncertainty is compounded by the fact that no one is able to pre-estimate how the economic crisis will turn out. Two scenarios are hotly discussed:

The crisis as a U-shaped curve with a longer stay at a flat level or the scenario of a V-shaped curve hoped for by many with an equally speedy growth once the crisis is over. Or does this crisis mark a break in the era?

What makes the corona crisis so elementary, is the fact that the entire economy including all its players is facing fundamental changes which cannot be fathomed at the moment. The financial crisis and the near-catastrophe of 2008 did not result in a new world order; everything was done to restore the status quo as quickly as possible. The populist revolts against globalization had little effect on the interdependencies of the global economy. The corona crisis, however, has the potential to magnify the geopolitical and economic breaking points of our times. The crisis did not create the trend for de-globalization; its shockwaves could, however, help bring the shifts that have been working in the dark for some time into the light for good.

## The end of globalization as we know it?

The world that could result from the corona crisis could fall into rivaling blocks – this does not mean a fallback into the Cold War mentality. The global economy will still be intertwined. Economies could join together under the leadership of a regional power to ward off unwanted competition through incompatible norms and standards, technology platforms and communication systems, barriers for market access and infrastructure systems.

Thus, there is nothing less at stake than Europe's solidarity and unity and the positioning of the European companies. Germany in particular will have to fundamentally rethink its economic model. Shorter supply chains e. g. with production facilities in Eastern Europe could be less susceptible to crises. To remain technologically independent, the European cooperation in research and development would have to become much closer. In all areas the common market should be shaped into a political union without the old German fear to overwhelm Germany as a location for business by European transfers. In a globalized world there will be no national export world champions. Thus, the European market will become even more vital to the survival of the German economy than ever.

## Using the crisis as an opportunity

All companies are facing a (fundamental) struggle for survival; they will be forced to review and, if necessary, realign their strategies, activities as well as their entire ecosystem. An analysis of the overall business model will play a vital role in this. The future success in business will have to be significantly gauged by the old question: What is core business and what is non-core?

As soon as the companies have dealt with securing the company's existence short-term and thus sorted out their and the stakeholders' most existential questions, the idea will take shape that after the crisis will not be before the crisis. All companies, and German medium-sized companies as well, will have to tackle the question what their business model for the time after the corona crisis will look like and how it can be shaped. The entrepreneurs, managing directors, CEOs, advisory and supervisory board are facing a difficult task: How can the image of the future be shaped without any reliable parameters of what the future will look like?

At the moment, all parties are still hoping that the crisis will be a short-lived episode. However, the scenarios are different: Will the sudden standstill be followed by an equally steep increase or will the western global economies slide into a longer recession with little or no growth? Which conclusions will the companies draw from the susceptibility of the global supply chains?



# Challenges for German medium-sized companies

In the coming months German medium-sized companies will have to ensure their strategic and operative freedom of action in times of crisis. The economic lockdown will ruthlessly display the companies' weak points and become a matter of survival for many. Thus, all companies should use their time to critically question their business model and shape scenarios for the future.

A 3-step program could look as follows:

## 1. Ensuring the company's economic survival

Successful companies react to the corona crisis promptly and directly. A de-doubling from global and national developments is utterly impossible. The creation of a type of „corporate nerve center“ is recommended to obtain a comprehensive overview of the situation and make and orchestrate vital decisions. This decision panel should be kept small personnel-wise, be authorized to make and implement vital decisions and feature excellent communications skills: Transparency is key and channels the employees' fears and worries!

## 2. Taking critical stock of the existing business model

In a subsequent step all previous business activities should be subject to a rigorous stress test. What made the company strong in the past? How were the supply chains organized in the past and which supply chain partners will still be available after the crisis? The same applies to the customer side: which customers (B2B) will survive the crisis and will still be available as buyers? In the B2C-business similar things apply: What will the sales channels look like in the future? Which trading partners did survive?

## 3. Shaping the picture of the future in uncertain times

All companies will face a fundamental challenge: How to shape the future, if the parameters for planning and recognized planning models are not known? The planning process of the past cannot be applied to the future. Rather, the company and the entrepreneur will have to approach the new reality step-by-step and seize opportunities.

For many companies – should they survive the crisis economically – the business model will not really change. These companies are focused on a product, a technology or a service and have developed their core excellently and in many cases to (global) market leadership.

The core of a company is the essence of what distinguishes the company from others i. e. the main reason for the existing edge over the competition. This core does not have to be the company's most important product or service. It does not have to be the most important market in which it is active. Outstanding companies are characterized by their focus on successfully adding value. Often they are able to assert and expand their position in the market by consistently tapping the full potential of their core business and following recipes for growth that were tried and tested in the past.

Many companies tend to invest most into their weaker business fields. For business leaders it will be vital to identify those areas of business that cannot realize their full potential - be it in terms of customer segments, cost positions or competitive disadvantages. After 10 years of steady growth there are enough examples of diversification among medium-sized companies. The corona crisis will mercilessly identify such parts of the company and, unless they significantly contribute to the company's success, pose the question: What will be core business in the future and what will not? Just as important is the communication of the image of the future with its core activities. But an open communication of „no-go's“ within the organization is also of great importance.

## Shaping the image of the future independently – M & A and portfolio management as a factor of success for increased value and growth strategies

The German industry is faced with extreme challenges. Strategies will have to be reevaluated and perhaps redefined. Areas of value creation will be reshaped and require flexibility and decisions. Medium-sized companies and their management will be forced to answer the question of sustainability for themselves and maintain their freedom to act. The corona crisis will not leave any time resp. room for existential questions; the pressure to decide and act will increase with each additional week of the lockdown.



**Under this assumption the following applies to all companies:**

### **1. Make fast decisions**

All entrepreneurs will be forced to answer the question of economic survivability not just based on the status quo of previous business and strategic activities but rather based on an altered future. Essential decisions should be made as soon as possible while the full freedom to act still exists. Even in uncertain times a corporate transaction is still conceivable when achieving a reasonable transaction volume to ensure the future and a successful continuation of the business.

### **2. Focusing on the core and growth**

Even in the times of the corona crisis growth is possible and achievable. Turbulent times require creative strategies. Entrepreneurs should also think about where they come from what exactly their core business is. Successful companies focusing on their core business follow 4 principles:

- They have a clearly defined core business and know why this business is successful.
- They follow clearly defined principles and convictions regarding their business model.
- They have an efficient leadership structure with few levels of management that are authorized to make decisions.
- They have a powerful feedback system and few operative and well-known performance parameters.

Once the management has reached consensus regarding the core activities of the business, a prudent organic growth into closely related business fields based on proven and repeatable recipes for success may be supported in a focused manne – also by purposeful acquisitions, to tap the full potential for growth.

### **3. Sale of non-core activities**

Active adjustments of the portfolio and the related divestment of non-core activities are the trend at many companies. These M&A-activities referred to as carve outs have in recent years become an essential component of strategic positioning. The high liquidity of private equity investors and strategic buyers permits targeted M&A-transactions even in times of economic crisis. Particularly in uncertain times financial investors and cash-rich companies are able to assume the role of an industrial consolidator and lower costs by investing in technologies and markets and create unique market positions in the long run.



## Sound advice in difficult times

Even in economically good times the decision to sell the company is the economically and emotionally most important decision in the life of an entrepreneur. But in times of crisis the sale of a company or parts thereof is part of a responsible corporate policy and ensures the survival of the business. Particularly in times of crisis the decision to sell should be made in good time and out of one's own free will. Comprehensive competent guidance by professional neutral advisors may help to significantly increase the value of a transaction even in corona times.

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