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PANEL 2. BEST PRACTICES IN INDUSTRIAL RESTRUCTURING IN ECE COUNTRIES –
SECTORAL AND TERRITORIAL ASPECTS

Topic 3. Restructuring ailing enterprises, industries and sectors

THE RESTRUCTURING OF THE RIESA STEEL AND ROLLING MILL*by Mr. **Juergen Kuehn**, Director General (ret.), Federal Ministry of Economics
Germany**1. Steel market of East Germany**

Following Germany's unification the steel industry of East Germany undertook far-reaching restructuring measures. In 1989 the East German steel industry produced 8 million tons of crude steel with a labour force of about 80.000 people. In 1995 the production was reduced to 3,9 million tons with an employment of some 7.000 people. Within a period of six years the steel production had gone down by more than half and the work force had been reduced by more than 90 per cent.

2. Outdated Riesa steel structure

Among the three biggest iron and steel metallurgical combines in East Germany the Steel and Rolling Mill Company in Riesa/Saxonia faced particular severe problems. It had been founded in 1843, became part of the famous German steel trust Flick and was completely dismantled after the Second World War. Reconstruction started in 1946. The steel production reached 1,2 million tons in 1981, but declined in the following years and amounted to 680.000 tons in 1989.

* This paper is presented as received from the author.

As a result of many years of neglected investment in central sectors the plant's technological equipment was completely outdated, even when compared with other East German steel producers. The major part of the company's output was produced by Siemens-Martin furnaces, a process everywhere else discontinued since the 1980's because of the high energy and capital costs.

In addition, the company had to overcome several handicaps:

- The combine maintained specific internal capacities for a wide range of activities not directly related to the main production line, reflecting the general policy objective of achieving self-sufficiency and avoiding interferences from the outside.
- Additional responsibilities were placed on the company, e.g. residential construction work and power supply for the region.
- The potential of modernising the machinery, the equipment and the appliances had been completely neglected.
- High maintenance and repair capacities had to be kept up in view of the poor technical status of all material. The degree of wear and tear in equipment has been put at almost 70 per cent. It represented the highest rate in the three major metallurgical combines in East Germany.

The situation became even worse by the breakdown of the traditional East European markets and the world-wide recession of the steel industry.

3. Employment situation

In employment terms the Riesa Steel and Rolling Mill had the greatest number of workers in the East German iron and steel industry. In 1989 it employed some 12.000 people of which more than a quarter were women. Some 40 per cent of the work force were engaged in the central production, about 30 per cent in maintenance and subsidiary sectors, 15 per cent in planning, accounting, statistics, safety and training, 15 per cent in science, research and technology, in social affairs and in quality control. Most employees disposed of high career qualifications. Specialized experts with college or university degrees worked in all sectors. The company was the greatest employer in the region. Through its activities it influenced the public life well beyond the city limits.

The structure of the employment gave an indication of the low degree of production efficiency:

- The great number of administrative personnel reflected the planning bureaucracy in the company.
- The wide spread of business prevented a concentration on the core activities.
- A large part of the employment was engaged in keeping up outdated technological installations.

4. Reasons for breakdown

Summarizing the main element for the lack of competitiveness in 1990, there were three internal and three external reasons. Internally, the company had a low labour productivity, its production costs were too high and the quality did not meet world market standards. Externally, 80 per cent of the production went to markets in East Europe and were not any more disposable, whereas 20 per cent could be exported to the West

only under dumping conditions, there was a collapse in prices and, finally, consumers were not able to pay for their purchases.

5. Alternative choices

After the unification of Germany these disadvantages quickly led to a strong decline in production. In 1990 the "Treuhandanstalt" (Trusteeship Board), the new owner of the company, nominated a new Managing Board and selected the Members of the Supervisory Council. The Supervisory Council consisted of 11 Members, of which 5 represented the owner, 5 represented the employment, plus 1 neutral Member. Immediately after their appointment the Managing Board and the Supervisory Council realized that there were no potential investors interested to buy the company as a whole single unit on the existing site. Therefore a privatisation of the complete plant was not possible and the decision-makers had to make a choice between two alternatives: either to restore and to modernize the plant or to liquidate the company and to stop all production. Both decisions would have had the most serious repercussions. The complete renovation of the establishment could only be effected by a permanent flow of State subsidies, whereas the the total stop of output and the pulling down of all technical equipment would lead to the loss of several thousands working places and, at the same time, create very serious economic problems for the whole region.

6. New Concern Strategy Plan

After very careful examination and consideration the Managing Board and the Supervisory Council concluded that the liquidation of the company, combined with a complete new Concern Strategy Plan, was the only realistic approach offering a chance for the revival of the region. The objective of the strategy was the transformation of the old Riesa steel plant into a modern industrial area. On the traditional steel site a new assembly of efficient business activities was to be established with the aim of being competitive under global conditions.

Pre-conditions of the restructuring policy were:

- The disposal of sufficient public resources to promote employment during the demolition period.
- Financial assistance for reconstructing under the auspices of the European Coal and Steel Community.
- Confidence between the workers, the management and the public authorities.

The Concern Strategy Plan consisted of five major parts:

1. Privatisation of single sectors of interest to individual investors, e.g. pipe mill, parts of machinery and engineering, scrap processing.
2. Utilisation of non-productive assets, e.g. holiday homes, health and child care facilities.
3. Establishment of metal processing companies, e.g. mini-steel plant with rolling mill.
4. Re-development of areas and buildings, creation of new infrastructure.
5. Training and re-training of workers for new jobs.

The transformation was implemented step by step in a series of parallel processes. First of all, the metallurgical production had to be stopped and the plant equipment dismantled and demolished so that scrap could be produced.

The next stage consisted in re-developing the site and the installations as well as in qualifying the personnel for new employment sectors. All these activities contributed to the creation of a complete modern infrastructure. Finally new companies were founded and set up on the site. The different steps were taken in a span of six years, from 1990 to 1995.

In retrospect, when looking back at the complete restructuring process, I consider the rather courageous decision taken at the beginning in 1990 as the the most important directive influencing all subsequent stages of restructuring.

7. Main elements of the restructuring policy

For the revitalisation of the industrial area of 78 hectare and for the modernisation of the infrastructure a total of 204 million Deutschmark (104 million EURO) have been invested. For each newly created job public funds of the amount of 180.000 Deutschmark (92.000 EURO) were utilised. Newly settled companies provided investment pledges totalling 420 Deutschmark (215 million EURO). Between 1991 and 1995 radical changes in infrastructure resulted in the creation of a modern industrial site, including

- the demolition of old buildings
- the modernisation of other buildings
- the construction of new production facilities, including the setting-up of a modern mini-steel plant
- the creation of a new technological and transport infrastructure, including the construction of a public road network with a total length of 3,6 kilometer.

More than half of the new companies were established by splitting off selected sectors of the Riesa Steel and Rolling Mill. Examples were

- the Mannesmann Pipe Works
- the Qualification Center Riesa
- the Construction Union Riesa
- the Rhein-Ruhr Steel and Container Building Company.

About one quarter of the new companies were founded on the initiative of companies in West Germany. More than 10 per cent of the new companies originated in Italy, Switzerland and Austria. The most prominent example is the Italian mini-steel plant Feralpi which will turn out about 70 per cent of the re-enforcing steel produced by the former company. Its production represents the latest development in steel technology. The market prospects are seen as very favorable. Another example of a new foreign firm is the Swiss central heater company Arbonia-Forster whose production benefits from the home buildings activities in East Germany.

8. Employment effects

Right from the beginning of the restructuring activities, the Concern Strategy Plan has been the subject of intensive discussions with the workers. They accepted the critical prospects of the future development of their company and were willing to contribute to the the total transformation of the site. Their engagement was supported by the Metals Workers Trade Union and financially assisted by labour market policy measures of the Federal Government. Employment contracts with limited duration were concluded for about 2.600 workers to re-develop the site as a start-up for new business. The feeling of "being needed" was of considerable

psychological importance. There were only a few demonstrations and the workers council followed the whole process with a positive attitude. In general, social peace was maintained in the Riesa area.

From 1990 to 1996 the original work force of 11.524 employees has been gradually reduced step by step. At the middle of 1995 about 3.600 workers had been taken over by new enterprises. Older employees beyond 54 years of age benefitted from early retirement arrangements. No alternative employment could be offered on the site or at other locations for about 2.000 workers (about 18 per cent of the former work force). Their contracts were terminated providing for compensation payments on the basis of social plans. Men and women were equally affected.

About 70 new companies settled on the site, planning up to 5.020 jobs. Taking synergy effects into account, a total of 6.000 new jobs have been created. In the final stages about 50 per cent of the former steel work employees have found a new occupation as a result of the conversion of the area.

9. Summary and conclusions

The decision for restructuring the Riesa Steel and Rolling Mill was taken at a time of great political and economic changes. In view of the company's limited competitiveness and the shrinking chances on the international market the old structures had to be replaced by new, more efficient facilities. At the center of the modern strategy was the establishment of companies in the metal processing trade, equipped with high-tech tools, and the production of goods in strong demand. Private ownership of the new companies facilitated this development. In all stages of restructuring not only the overall economic effects, but also the individual employment results were taken into consideration. The restructuring process was successfully concluded with the transfer of about half of the former employees to new structures at the site of the old company. There were substantial synergy effects in the local and regional economy. The restructuring process contributed to the stabilisation of the purchasing power in the region.

The restructuring of the Riesa Steel and Rolling Mill has been regarded in Germany as a model for other restructuring exercises. The main features of this model have been summarized as follows:

- The coordinated approach to a large number of individual restructuring steps
- The market analysis of the need for changes
- The flexible concept and the high degree of engagement of the management in cooperation with the employment and the public authorities
- The intensive marketing effort to win and to support new investors
- The regard for investor's interests in modernizing the site
- The active participation of workers and their Trade Union in the restructuring process.

In a study on the Model Riesa two German experts concluded their findings by the following sentences:
"Experiences gained from the Riesa process may be applicable in East European countries which need to restructure their economy. It is, however, important, in the run-up to such developments, to work out and implement the necessary pre-conditions, such as political labour measures parallel with job reductions, to ensure that economic success is not impaired by social conflict situations".

