IPO Governance Case

by Jean-Pierre Jeannet
(USA/Switzerland)

Babson College
IMD

Orthotec was a privately held company manufacturing surgical tools for orthopaedic surgery. Founded by Thierry Monnet and Serge Begulin, two engineers, its products required sophisticated and state-of-the-art machinery to shape the metal parts to the high requirements of orthopaedic surgery. Customers were orthopaedic implant companies that packaged their implants with the surgical tools and distributed them to hospitals worldwide. Since its foundation some 30 years ago, sales had reached about CHF 50 million with average profitability for this industry.

About 15 years ago, the original founders had looked towards an exit strategy and engaged Christian Volland as executive and CEO with medtech industry experience. When entering the company, Volland was able to acquire Volland's 50% stake in the firm and Monet continued as shareholder.

The company then grew from about CHF 2 million to CHF50 million under the leadership of Volland. Originally, the company had a majority of its activities in the machining of advanced components for the watch industry. With growth prospects in the medical sector judged much more favourably, new ownership decided to pivot the company into the medtech space and pursue implant OEMs aggressively. The rapid growth was both a managerial and financial challenge.

When the remaining founder, Begulin, wanting to sell his stake, caused some difficulties for CEO and co-owner Volland who suddenly was faced with having to find not only new capital for growth but also replace a retiring founder. Volland viewed a strong potential for the firm to double in size with a possible acquisition that would expand the product line from niche towards full line and also offering metal cases for tools that could be carried into the hospital operating rooms.

After a lengthy search for replacement capital and funds for growth, Volland had attracted some local private equity firms who were prepared to share the investment doubling the company's value from CHF 25 million to 50 million. Given investment

limits, none of the local PE funds could shoulder this deal alone. A distributor in Europe was acquired and had been paid for with shares. With the new capital, and an acquisition to boot, the company expected to reach sales of about CHF 200 million and eventually go for an IPO valued at above CHF 250 million, a substantial return for all equity owners. Although Volland and one of his key executive together owned slightly more than half of the equity, they had to accept three outside board members to join Volland and his colleague.

One of the largest OEMs and a major client of Orthotec were looking to sell one of its plants to Orthotec together with a multi-year sales contract for existing products. Volland saw the possibility to rapidly move towards the eventual goal as the industry players were moving rapidly towards outsourcing complete surgical tool sets from suppliers, rather than pick them one by one and assembling kits themselves. Volland signed an agreement in principle with the OEM. To complete this transaction, he required a bank loan of CHF 20 million combined with a capital increase of CHF 5 million. A bank stood ready to lend but then suddenly rescinded its commitment.

When Volland convened his board of directors, he was surprised to face resistance. Among his private equity investors, the lead investor was very hesitant and argued that he was not sure that Volland was the right person to take this company to the IPO level and that Orthotec should first completely digest the previous, small, acquisition. After a long debate, the board consisting of Volland and his senior executive, as well as three outside investors, finally decided that Volland could close the deal but there could be no capital increase, and the board would want to monitor every step of the discussion and negotiation taking place. The lead investor even announced willingness to sell its stake.

At this point, Volland faced some very tough choices. Under the present situation, he could not go through with the deal, which would make him loose face with his major customer, a situation he wanted to avoid at all costs. He might find another lender willing to accept step in, but with a deadline looming of 3 months out this appeared difficult. He was considering finding new investors to buy out those unwilling to go further. Another possibility arose with some competitors who signalled interest to do a trade sale. Volland was wondering how to best salvage the possibility of an eventual IPO down the road with the chance of a higher return on the invested equity.

Epilogue

With the expiration of the purchase agreement with the major OEM just 3 months away, Volland was hesitant to pursue options that would take a long time and possibly not be realizable. He did not think the new investor route would be realistic within the deadline, and the new bank/lending agreement might be risky to conclude as well. Ending with no deal in place to acquire the offered plant felt like the worst-case scenario to him. In the end he concluded a trade sale, which he could, with a

majority of shares and a drag along agreement with shareholders. This sale did not yield much more than the earlier valuation from the entry of the PE investors. Worse, the new owner did not grow the business, and the prospects of a much larger company fizzled. Employment in the Orthotec company main plants shrunk, leaving everyone a loser compared to earlier growth prospects.

Open Access This chapter is licensed under the terms of the Creative Commons Attribution 4.0 International License (<http://creativecommons.org/licenses/by/4.0/>), which permits use, sharing, adaptation, distribution and reproduction in any medium or format, as long as you give appropriate credit to the original author(s) and the source, provide a link to the Creative Commons licence and indicate if changes were made.

The images or other third party material in this chapter are included in the chapter's Creative Commons licence, unless indicated otherwise in a credit line to the material. If material is not included in the chapter's Creative Commons licence and your intended use is not permitted by statutory regulation or exceeds the permitted use, you will need to obtain permission directly from the copyright holder.