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Resurrection of companies 2012 – Profit generators or zombie firms?

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1. Summary

In 2011, greater efforts were spent on the financial restructuring of firms controlled by the banking system. The restructuring of numerous larger firms is now complete and, in many cases, their sale has been finalised. In the opinion of the Competition Authority, the banks' control of undertakings has been significantly reduced, although there is still some way to go.

Icelandic firms are extremely leveraged in international comparison. It is noteworthy that the debts of firms that have completed their restructuring remain quite high. Approximately a third of the managers of larger Icelandic firms that have been sold and restructured consider that their firm cannot meet its current debt obligations, or that it is unclear whether it can meet such obligations.

The Competition Authority is of the opinion that there are numerous risks posed by leveraging companies too highly. Undertakings that are highly leveraged can neither provide competitive restraint nor operate efficiently in the market. There is a risk that such companies decide the price of their goods or services in accordance with their poor debt position, if at all possible. This risk of this becomes ever greater the less the competition in the market in which the firm operates and the greater the market share it has.

It is important that the debts of companies that have a sound operating basis are adjusted to their payment ability and their ability to return a profit. A healthy economy is the foundation by which the growth and development of the banks must inevitably be governed. An over-leveraged business sector, therefore, benefits neither the long-term interests of the banks nor the economy.

In the near future, the Competition Authority plans to direct its attention to two aspects in connection with its monitoring of company restructuring; on the one hand monitoring the profitability goals of firms controlled by the banks and, on the other, ensuring that the banks' actual control of firms is transparent. Requirements for profitability are intended to reduce the risk of banks funding costly marketing efforts that make it possible for the overtaken company to grab an increased market share in the market in question, and maybe even drive its competitors out of business.

The Competition Authority has recently been examining several cases where bank control of companies, according to competition legislation, is considered to have developed. This is a particularly important question at present in light of the high leverage of companies and the ability of banks to have an impact on the operation of undertakings through terms in loan agreements and provisions for calling in debts.