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The Chicago Ownership Conversion Project Transition to Transformation

Purpose: To help retain Chicagoland's industrial base by arranging the acquisition of manufacturing companies through ownership succession by groups of employees, African American or Hispanic men and women, and High Road entrepreneurs. While primarily focused on smaller, privately-held companies, this effort may extend to deal with similar opportunities with larger companies as well.

Manufacturing Renaissance, Safer Foundation, the Local Initiative Support Corporation Chicago (LISC), and the Chicago Federation of Labor (CFL) are the partners in this project. The Safer Foundation and Manufacturing Renaissance are the managing partners of this initiative until the new entity is launched. Dan Swinney serves as the Interim Director.

The Opportunity

Today, hundreds of manufacturing companies employing thousands of workers in the Chicago region are in danger of closing because of the absence of successors¹ to retiring owners. This demographic shift, referred to as "The Silver Tsunami" is a crisis that can be a transformational opportunity. It can change the traditional ownership structure in manufacturing from a white, and male private sector to a sector that includes workers, as well as Black and Hispanic men and women as owners. This change also creates the opportunity to alter the values that guide the management of the manufacturing sector from one that is exclusively focused on private accumulation of wealth to one that addresses social problems as it generates a strong ROI.

In 1989, Manufacturing Renaissance completed a study for the Economic Development Commission Foundation of Chicago that looked at 800 small companies with a principal of 55 years of age or older. 40% of these companies were in danger of closing because they had no apparent successor. We believe the conditions today are the same. We have hired the Great Cities Institute at the University of Illinois to update this important data. This research project is under way and funded by the Chicago Community Trust.

In Cook County, there are 6,272 manufacturing companies employing 185,500 people. There are potentially 1,500 to 2,000 companies at risk due to the succession gap.² Recently, *Crain's Chicago Business* described succession challenges and opportunities for millennials.³ In a report by the Ohio Employee Ownership, it was noted that, "The failure to plan for business succession in small and

¹ <http://mfgren.org/wp-content/uploads/2015/10/Succession-and-Aging-Mfg-Owners-1989.pdf>

² US Bureau of Labor Statistics Quarter 4 2016 report

³ "When Suddenly the Kids are in Charge," *Crain's Chicago Business*, November 28, 2016, p. 3.

medium-sized companies is the leading preventable cause of job loss in the United States.”⁴ As stated in a recent report issued by the Budget and Tax Center, “Estimates vary, but it is likely that upwards of 4 million companies owned by baby boomers will be sold or dissolved by 2030 leading to the transfer of roughly \$10 trillion in business assets. While the Great Recession forced many baby boomers to delay their plans to sell and retire, we are on pace to see more small businesses change hands in 2016 than any year since the start of the Great Recession.”⁵

This is a long-standing problem in Chicago and around the country. Small, privately-held companies are hidden in plain sight. There is relatively little information about the particular companies. Issues of succession of ownership are seen as a private family concern. Another major consideration is the fact that manufacturing companies are overwhelmingly owned by whites. According to *Crain’s Chicago Business*, 99% of Illinois manufacturing companies are white-owned—separating large pools of entrepreneurs from consideration in the acquisition of manufacturing companies. Larger, publicly traded manufacturing companies are often at risk because of short-term pressures from Wall Street and can also represent opportunities for acquisition—particularly those with union representation.

The Project

Our central objective is to identify manufacturing companies with a succession challenge and match the company with a qualified buyer of the company offering a fair and acceptable price and terms for the owner. We will assist in the financing of the acquisition through our own fund that will provide debt and equity. Once the acquisition is complete, we will continue to work with the company to ensure its success as a business enterprise, including becoming part of a network of companies committed to the values and priorities of the Chicago Ownership Conversion Project and its partners. This project is not the “silver bullet” that will solve all the challenges of our region—but it is a key part.

Building the Business Prospecting Network: Key to the success of this effort is the identification of prospects when they are healthy, viable companies. We will systematically gather information from people who work in companies through unions, community-based organizations, churches, the local development community, and service providers for the manufacturing sector. The Chicago Federation of Labor, Manufacturing Renaissance, and LISC will reach out to their affiliated organizations and networks to find help in identifying company prospects. Identification of a company with a possible succession challenge will lead to research and discreet outreach to the owner to see if a sale is possible. Research will continue to determine if the company is viable and capable of growth, as well as determining a fair price for the company. If the company is viable and available for sale, the search for a qualified buyer will proceed.

Developing Pools of Qualified Purchasers: In addition to retaining manufacturing companies and jobs, the objective of this project is to diversify ownership in the manufacturing sector. We will develop a pool of people with the skill, financial means, and desire to purchase companies. We have a particular interest in exploring the potential for employee ownership through the cooperative model or through an Employee Stock Ownership Plan. We also have a particular interest in developing our ties with African American and Hispanic women and men entrepreneurs that have historically been left out of this sector. Specifically, we will work with groups of employees as well as African American and Hispanic

⁴ Ohio Employee Ownership Center. “Exit Planning.” <http://www.oeokent.org/exit-planning/>.

⁵ “Down Home Capital: How Converting Businesses into Employee-Owned Enterprises Can Save Jobs and Empower Communities” by Patrick McHugh, Budget and Tax Center.

men and women to acquaint them with the opportunities that are available to them in manufacturing acquisition, to help them learn and acquire the qualifications and resources to be engaged in acquisitions, to introduce them to sellers, and to assist them in the transaction. Developing these pools of entrepreneurs will require dedicated staffing. The Safer Foundation, LISC, and Manufacturing Renaissance will play leading roles in this aspect of work.

We will also seek partnerships with banks, private equity funds, social investors, and traditional entrepreneurs committed to patient and long-term investment as well as acquisitions in manufacturing as long as their objective is to sustain production and treat the workforce and key stakeholders fairly. We believe the demand for new owners of companies will quickly exceed the pool of those interested in being part of an acquisition so the broader the pool of partners who share the same values the better.

Identifying sources of capital: Many of these types of acquisitions can be conventionally financed by existing owners, banks, and new owners. We will create a fund dedicated to this kind of transition and willing to provide patient and reasonably-priced capital for the acquisition of these companies as well as the continued development. We will seek active partnerships with Chicagoland's financial community.

Policy: We will seek supportive policy at the local, state, and national level. In recent weeks, we presented our project to the Cook County Social Innovation Commission and to a forum hosted by them on October 4. Our project was also covered in an article in *Crain's Chicago Business*.⁶

The Stages of Development

The Development Stage: We are currently in the development stage of this project that includes updating our research on manufacturing companies facing a succession challenge and that might be an acquisition opportunity; sorting through the various legal questions associated with this kind of unique partnership and organization; building the partnership and division of labor between the four lead organizations; and developing a business plan that will guide our decisions regarding the legal structure for this initiative, our recruitment for staffing, our partnerships and our financial plan. With this work completed, we will form the new entity, hire staff, and get to work in identifying prospects and matching them with qualified entrepreneurs.

The New Organization: With the new organization, we expect to have a small highly qualified and experienced staff to carry out the work of this project. The Managing Director will have a background in acquisitions, management, and provide overall leadership. The Development Director will have extensive acquisition experience and be responsible for determining the viability and value of companies, qualifying owners and purchasers, and closing the deal. The Prospecting Director will be identifying opportunities for acquisition through our contacts with manufacturing companies and

⁶ http://www.chicagobusiness.com/article/20170927/NEWS05/170929888/how-to-get-more-women-minorities-to-own-manufacturing-firms#utm_medium=email&utm_source=ccb-dailyalert&utm_campaign=ccb-dailyalert-20170927

associations, the labor movement, community based organizations, and Chicagoland's vast community development network. The directors will be supported by additional staff. We will also rely on consultants and others for legal assistance, research, and outreach including our core partners.

Although operated as a non-profit according to the principles and goals of MR, Safer, the Chicago Federation of Labor and LISC Chicago, this organization will be structured like and perform many of the same functions as a traditional investment banking company involved with mergers and acquisitions including making direct investments in companies. We are seeking funding to launch this organization and then expect the revenues from transactions to largely finance its ongoing operations. The transaction revenues will include a combination of approaches such as a percentage of the financing using the standard Lehman Formula,⁷ retainers, consulting fees prior to and after the acquisition, and on-going pay-out from the profits of the company. We will rely heavily on the foundation community, financial institutions, and government at the local, county and state level to fund the Development Stage. We expect our fee for service revenue to grow substantially starting in year 2.

A draft budget for the next three years is attached. This will be refined through the Business Plan.

Conclusion

We think this project presents a unique opportunity for innovation in the field of economic and community development. What we see as a crisis in ownership succession in the manufacturing sector creates an opportunity that combines community and entrepreneurial interests and leads to a broader, more diverse, and more stable pool of owners in manufacturing. This is a project that has the potential to generate revenues that can support other aspects of community, education, and workforce development. We are confident that this effort will have national significance.

⁷ This is a common formula in the merger and acquisition business for determining fees. Typically the Lehman Formula generates 5% of the first million dollars; 4% of the second, 3% of the third, 2% of the 4th and 1% for the subsequent millions in financing.

The Partners

The Chicago Ownership Conversion Project is an initiative of Manufacturing Renaissance, the Safer Foundation, and the Chicago Federation of Labor.

Manufacturing Renaissance: Manufacturing Renaissance (MR) has a 35-year history of engaging in the issues of manufacturing and ownership in the context of inner city communities and in partnership with local government, labor and community-based organizations. In this context, we were introduced to the possibilities and requirements of arranging a transition in ownership. We arranged several employee purchases of companies as well as acquisitions by entrepreneurs of color. We engaged in extensive efforts to prevent particular companies from closing by organizing an acquisition effort by employees with the support of their union as was the case with Brach Candy⁸ and Stewart Warner. In 1989, we created Chicago Focus, a for-profit subsidiary of MR, to arrange acquisitions by employees and minority entrepreneurs—a company that was active for 5 years. Central to success of our conversion efforts was timely and accurate information to identify prospects 2-3 years before they face a crisis. To meet this need, we developed a Business Prospecting Network that relied on gathering information on companies from labor, community and local businesses including companies facing an ownership succession challenge. We developed these systems in New York City and Chicago.⁹

Additionally, MR has developed the Manufacturing Connect high school program modeled on the experience of the poly-technical school of Mondragon Spain that educated the young people who formed the first cooperatives in the 1950s. We see this as the long-term approach to developing a pool of entrepreneurs. Our Manufacturing Connect program has enjoyed the support of 90 typically smaller privately-held manufacturing companies since 2007. The owners of these companies praise our interest in succession of ownership and are candid about the challenges they personally face in ensuring their company solves the succession challenge. This is a pool that we will turn to in this project.

The Safer Foundation: The Safer Foundation, founded in 1972, is one of the nation's premier social impact organizations focused on the support, education and employment of justice system involved youth and adults with arrest and conviction records. Safer Foundation provides a wide range of services including housing, behavioral health services, academic education, job readiness training, vocational training, job placement services and entrepreneurship training.

Preservation of manufacturing jobs is strategically important to Safer Foundation and our clients. Safer Foundation views the Chicago Conversion Project as a critical need to ensure Illinois does not lose manufacturing companies and the important living wage jobs they provide. In addition, as has been stated earlier, the operation of manufacturing companies in the local economy creates exponential economic benefits our local communities sorely need.

During 2016 Safer Foundation launched the Aspire Entrepreneurship Program. The Aspire Entrepreneurship Program, funded by Kellogg Foundation and Justine Petersen, prepares our clients to launch and operate small businesses. A local extension of Safer's work is to assist clients with entrepreneurial aptitude and interests to successfully operate businesses. Small businesses are the number one creators of new jobs in the US economy. People with records who launch their own

⁸ <http://mfgren.org/wp-content/uploads/2015/10/Misadventure-in-Candyland-Part-1.pdf> and <http://mfgren.org/wp-content/uploads/2015/10/Misadventure-in-Candyland-Part-2.pdf>

⁹ http://mfgren.org/wp-content/uploads/2015/10/early_warnings.pdf

businesses are then in position to extend employment opportunities to others who have similar life experiences.

The objectives of the Chicago Conversion Project; the preservation of manufacturing businesses and manufacturing jobs in the local economy, is consistent with the strategic goals of the Safer Foundation. Safer Foundation is committed to the success of this project as a means of preserving employment and business ownership opportunities for our clients.

The Chicago Federation of Labor: The Chicago Federation of Labor was founded in 1896 as a way to strengthen the efforts of individual local unions by creating a unified voice for the labor movement in the Chicago area. Chicago is considered by many as the birthplace of the American labor movement, home to more “Local 1” unions than any other city and the movement for the eight-hour day. As of today it represents around 500,000 workers in Cook County including a number of unions and members in the manufacturing sector.

The CFL is a leading voice in the American Federation of Labor and Congress of Industrial Organizations (AFL-CIO) and was a founder of the Chicagoland Manufacturing Renaissance Council. In its effort to retain Chicago’s industrial base, the CFL decided to actively join the team of the Ownership Conversion Project. Its member unions will play a leading role in identifying prospects for acquisition.

The Local Initiatives Support Corporation (LISC): LISC was founded in 1979 by the Ford Foundation to provide grants, loans and technical support to advance community development. Since then, LISC has become a leading nonprofit organization in community development, active in 30 cities and a rural program. It provides expertise, technical resources, financial resources and a professional network to neighborhood organizations working to improve their communities.

LISC Chicago’s mission is to connect neighborhoods to the resources they need to become stronger and healthier. That mission is achieved, in part, by emphasizing certain values such as stewardship, coordinated action and commitment. LISC is active in nearly half of the city’s community areas.

The objectives of the Conversion Project align with LISC’s mission to have stronger and healthier neighborhoods, particularly to transform locally developed goals into visible, positive change for people and places. As such, the organization will play a leading role in arranging the financing of specific acquisitions in the Project.

How to get More Women, Minorities to Own Manufacturing Firms

By Lisa Bertagnoli

September 27, 2017



Dan Swinney, executive director of Manufacturing Renaissance, one of four nonprofits leading the Chicago Ownership Conversion Project.

As many as 2,000 small local manufacturing firms could be up for sale in the next decade. Four local nonprofits want minority and female entrepreneurs to buy them.

The Chicago Ownership Conversion Project aims to correct a “demographic crisis” in manufacturing by finding African-American, Hispanic and female buyers, as well as employee-led groups, for manufacturing firms headed by aging owners. The initiative, which is holding an informational breakfast Oct. 4, hopes to be active within six months.

A representative from one of the nonprofits says that manufacturing in Chicago has two problems: skills, which various workforce development and training groups are trying to solve, and succession. “That problem’s not been on anybody’s radar,” says Dan Swinney, executive director of Manufacturing Renaissance, which supports manufacturing and jobs in the city and is a partner in the conversion project. The others are Safer Foundation, which helps educate and employ people with criminal records; the Chicago Federation of Labor; and the Local Initiative Support Corp., a national nonprofit that supports community economic development.

The first step is “raising the issue,” Swinney says, noting that 99 percent of manufacturing concerns in Illinois are owned by white people. The project presented its plan to the Cook County Commission on Social Innovation on July 20. On Oct. 4, the commission will host the public breakfast and forum at BMO Harris Bank’s executive dining room.

In 1989, Manufacturing Renaissance research found that 40 percent of 800 local manufacturing firms with fewer than 100 employees and owners age 55 or older lacked an apparent succession plan. That study led Manufacturing Renaissance to arrange employee-led buyouts of several firms, including a now-defunct South Side printing shop and sausage maker Fred Busch Foods. In the coming decade, as many as 1,500 to 2,000 firms could be ripe for similar deals, Swinney says.

Great Cities Institute at University of Illinois at Chicago is updating the 1989 study to confirm those numbers. “This is a problem for our region,” Swinney says, noting that the baby boomer generation is aging and retiring. If smaller firms close rather than change hands, owners lose by not getting the full financial value out of their business, employees lose jobs, and the tax base suffers, he says. Finding minority business owners keeps manufacturing alive and also lets disenfranchised groups invest in their communities, he says.

The Chicago Federation of Labor will take the lead in launching Business Prospecting Network, which will identify privately held companies in Chicago that could close within a decade due to succession issues. It will also identify entrepreneurs and/or employee groups interested in buying the companies. The partners will launch a nonprofit, as of now unnamed, that will act as an investment banking company to arrange and help finance the acquisitions with long-term patient loans. The project needs about \$1.8 million to fund the first three years of operations. After that, philanthropy as well as fees generated from the purchases will support its efforts. Swinney says the organization will also seek to partner with banks, private-equity funds, social investors and entrepreneurs to help finance the purchases.

Firms closing after an owner dies or retires is a big problem in Illinois and nationally, says Jim Nelson, vice president of external affairs for the Illinois Manufacturers’ Association, a Springfield-based lobbying group. “An idea like this might have a good chance of succeeding, depending on the expertise the buyer is bringing to the table,” he says. The conversion project says it will find qualified buyers and work with them to ensure that the firm lives on as a successful business.

“This is pro-business, pro-labor and pro-community,” says Chicago attorney Marc Lane, vice chair of the Cook County Commission on Social Innovation, who is providing some legal support to the effort. “The commission sees this as a very significant initiative.” Lane says that the project is pursuing philanthropic and governmental funding, but he did not know if the county would help fund the effort.