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--
Changing Leadership Style to Accomplish a Turnaround

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By John M. Collard

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SECTIONS:

Article Text
About the Author
About the Firm
PDF Version

Steering Clear of the Brink:

Early Warning Signs Pinpoint Business Troubles— Changing Leadership Style To Accomplish a Turnaround

By John M. Collard

Whether you are an investor, serve on a board of directors, own or manage a company, you face business risks. All of the stakeholders accept additional risk when the company is heading for trouble. Balancing these risks can cause a predicament. By recognizing some early warning signs that indicate business trouble on the horizon, you can eliminate, overcome, or, at the very least, side step many of those risks.

Business trouble means different things to each of us at different times. The perception differs depending on the stakeholder, but the fear is always the same — loss of their investment (money, time, energy, good will, reputation). The anticipation of loss is unacceptable. No one likes to lose — anything.

Lenders, creditors, and shareholders may lose their investment. Owners can face financial ruin, disgrace, or humiliation. But worst of all, the employees have the most to lose. They can lose a life force, their income, and have little to say over the decisions that impacted that loss. In these times of miserable job

climate, stubborn economic recovery, and uncertain accounting practices, this loss can be the most devastating.

Top management is often aware that problems exist. The ‘trouble’ is, they wait too long to do anything about them. Why? Perhaps it's hope. ‘Things will get better soon.’ Perchance it's naiveté: ‘Management doesn't know how to manage in this situation.’ Maybe it's guilt: ‘If I'd been a better manager, I wouldn't be facing failure in the first place.’ Perhaps it's Founders Syndrome: The owner believes that only they, can run the company. But what is the most dangerous trouble of all? Denial [not the river in Egypt]. Denial makes owners or managers unwilling to admit that problems even exist. Or worse . . . it can blind them to the very problems that are heading their companies toward sure demise. Here's the bottom line: The longer it takes to get necessary help, the harder it will be to relieve the trouble and the more risk you assume.

When a company is in trouble, the rules change. Management is often ‘out of its element;’ it is entering untrodden ground. People haven't had to manage in this environment before. Why will they succeed now? The odds are that they will, at the very least, have difficulty.

Time and again, the obvious signs of business trouble are rarely its root causes. Losing money, for example, isn't the problem. Rather, losing money is the result of other problems. Diminishing sales, declining profits, mass employee exit, creditor suits, the threat of bank foreclosure, and no cash are only part of the equation. These problems can be repaired. The true dilemma becomes, who can handle the crisis management role?

All Leaders are not created equal

To save the company you must change the style of leadership to affect change. Clear thinking must prevail and a special set of skills must be applied.

If there is a qualified leader within the company, then delegate the job of turnaround to them, and provide proper support. If there is not a qualified leader in the company, and there usually isn't, don't hesitate to locate a professional at this type of work.

Let's put this leadership role into proper perspective. Leadership requirements differ between those for healthy, growing companies and for those in a troubled situation. The CEO that managed the company into trouble clearly is lacking the skills to doctor it back to health.

Contrasting Leadership Styles

Skill	Stable, Healthy or Growth Scenario	Troubled or Turnaround Situation
Focus	On Objectives	Survival, action, problem-solving
Decision making	Deliberate	Decisive, Immediate
Authority	Delegate	Direct Involvement
People	Develop	Recruit talent Communications
Respected for:	Management reputation	Financial credibility
Known for:	Consistency	Ability to shift gears

Differences in style are a key to success, in either situation. In the growth scenario, team building and coaching are buzzwords. But in the initial crisis and subsequent turnaround situation, *time is an enemy*. Decisive action is required.

The focus is dramatically different. This is one reason why the troubled environment is so foreign to many managers, and hence, the difficulty finding qualified talent from within the company. The stable environment allows for mistakes and longer lead cycles to achieve goals. Troubled companies have primarily one goal — to survive and get well. If the symptoms persist with no cure, the patient can die.

Companies often get into trouble because management procrastinates when it comes to making decisions. If the decision is made by default, it is akin to making no decision at all. Much of that early, and overall, survival also depends upon being immediate — upon making decisions in a timely manner. Even a wrong decision means movement and direction. If a decision turns out to be wrong, change it, but keep things moving.

Just as with a critical patient, the immediate focus at a troubled company should be on action — make something happen. The first goal in an absolute crisis is to stabilize and buy time. After calming the waters, take a reading on where things stand — which is normally still. Look for changes in ratios and trends to determine *what is*, or more importantly, *what is not* going on in the business.

Time is also an important dimension when it comes to authority. In a stable company, there is time to delegate and nurture the growth of the management team; time to work on long term issues and projects. In the troubled situation delegating takes on a different role. Managers must be held accountable not only for performance, but for timely results.

In a troubled situation, the decision maker must get directly involved. It is hard to worry about the long-term future when there may not be one. The leader is pressed closer to the immediacy of day-to-day operations. If you want action, request a decision . . . or make one.

In a stable situation there is time to develop talent. But when in trouble, remember that the good managers may have deserted the ship long ago, leaving behind the second string. You must exploit the talents of those employees that remain who can perform and bring them to new levels, then recruit talent that is lacking. It means building permanent management teams that can bring the company back to health — and add value to the company.

Communication is critical — with everyone who has a stake in the company's success. Talk to employees, but more importantly; listen to what they have to say. Be assured, they know when and where problems exist, and often have solutions.

A key element to a successful turnaround is to establish a good relationship with your lender. Capital is always required in tough times, not to mention that it’s nice to have in good times as well.

If the leaders who were in power while the company's position was allowed to deteriorate are still there, why should the lender believe that they would now be instrumental in correcting the situation?

To make matters worse, in the eyes of management, the lender is often viewed as an enemy instead of a key part of the turnaround equation. With all the suspicion that can surround a troubled company, it is important that trust be re-established with the bank. Credibility with the lenders is mandatory to success — and to keeping that cash flow at the bank. Since the bank holds the trump card, the institution must feel comfortable working with the turnaround leader. It means laying everything out on the table to keep the situation honest — and honoring commitments made to the lender.

Where consistency is important in a stable environment the name of the game in a turnaround situation is uncertainty. You can absolutely, positively count on surprises. "When it rains, it pours" may be clichéd, but when applied to a troubled company, one can be sure that “Murphy is shaking the clouds.”

The ability to deal with change at a rapid pace is essential. This is why a seasoned practitioner can be the answer to a successful turnaround plan, they’ve “been there, done that.”

The Process

Along with specific skills and an understanding of troubled situations, the specialist offers a new perspective from which to independently evaluate the company's circumstances. The process will focus on several issues:

- Is the business viable?

- Ø What is the purpose of the business?
- Ø Should it be saved? Why? Are those reasons valid?
- Ø Is there a core business that can be the source for the emerging business?
- Ø Are there sufficient cash resources to fuel the recovery?
- Ø Which existing managers are capable of leading parts of the company?

Remember, not all companies are salvageable.

The fact-finding must proceed as quickly as possible so that a realistic assessment of the current state of the company can be prepared. The specialist's first priority will be to manage cash flow — to stop the hemorrhage. Analysis of sales and profit centers, and asset utilization should indicate where the real problems — not the symptoms — are located. Next, a business plan outlining and suggesting possible courses of action — or cures — will be prepared.

Following this diagnostic stage, the transition can begin towards a turnaround. Most importantly, the leader needs to get things moving again. Once the course of action is chosen, implementation and monitoring can occur. The specialist should remain involved at least until the business is stabilized, and preferably until the transformation is complete and a new “Marquis” leader is found.

Who can help these besieged businesses?

Turnaround specialists generally are either interim managers or consultants. These leaders didn't start out as such — they were often managers that worked their way up the corporate ladder through hard work and (hopefully) fair play to build a solid management reputation. They have developed a set of skills to handle problem solving, getting results with minimal resources, (tight) cash flow management, negotiating and dealing with bankers, investors and creditors. The stakeholders will usually work with a turnaround leader — if he or she is credible.

Consultants are often a choice of the management team. Why? Because they are an advisor, they offer recommendations to management. Often the same management that guided the company into trouble in the first place. Why will they make those decisions now? Why risk allowing the same person to try again? Whether a consultant is effective depends upon management's willingness to *listen* and *implement* the specialist's recommendations.

The practitioner, by contrast, is a hands-on decision maker who actually takes control of the company—often as CEO—for a period of time. They are in control of the company's destiny, take the decision-

making reins, plot the course, and Steer the company through troubled waters, hopefully to safety. They must have an active line manager orientation, be decisive, isolate the problems and find solutions quickly.

Be assured there are countless cases where existing management agreed to work with a turnaround consultant only to placate the board or the lender. There is no substitute for qualified leaders with decision-making authority.

When hiring a turnaround specialist:

- Ø Check references.
- Ø Review proposals versus what can realistically be accomplished.
- Ø Require engagement agreements.
- Ø Hire an individual, not the firm - personal chemistry with the managers is critical.

A good practitioner has three goals; 1) get control, stabilize the situation, jump-start the turnaround, 2) develop and implement a sound plan, and 3) hire their permanent replacement, while working themselves out of a job.

Early Warning Signs

Too often, companies die unnecessarily. Why? Because, most lenders and managers haven't learned to recognize the symptoms of oncoming illness in their business.

When you wait too long to recognize deteriorating characteristics the company seeks bankruptcy protection . . . only attorneys and accountants benefit from this process. It's the astute lender or manager that recognizes infallibility, and has the foresight to ask for help . . . before serious trouble sets in.

Here are ten common signs that a company is heading for trouble. Carefully consider whether or not they apply. If you can answer *yes* to some of these questions, it is time to take decisive action.

Is the owner or top management over extended?

Whose work are they doing? When they continue to perform functions that should be done by others (once the business has grown to a more complex level), they're over extended. They should do the work for which no one else is qualified.

Managers need to delegate work appropriately. Define the owner's and key managers' jobs to clarify role responsibility. Assess subordinates' competence; retain them if appropriate — replace them if not. Monitor key metrics so you'll remain informed about conditions . . . without being immersed in them.

Relationships of how numbers behave tell the real story. The balance sheet is only a snapshot in time (what you have, what you will receive, and what you owe). The income statement indicates what happened during a given period. The source and use statement shows where cash went in and out.

But these financials don't indicate how to run the business. Movement must occur in two areas — on the *volume in* (revenue/sales) side, look at where and how revenue is generated. Is it from existing customers and contracts or new business? Most importantly, keep it coming in. On the *volume out* (throughput/ production) side, look at getting the product or service ‘out the door’. How else can you bill for it?

Is the turnover rate excessive?

A sure sign of underlying problems is rapid employee turnover. Employees know when problems exist, the good ones will leave early. This condition can be the result of a faulty hiring process, inadequate training, poor management . . . the list goes on. The price for ignoring this problem is high: low morale, lost wages, recruiting costs, lack of productivity, and ultimately, forfeited business.

Uncover the real causes early on, and rectify them. Solutions include clearly defined job responsibilities, performance expectations, rewards, and scope of authority. Several levels of management attention should be devoted to new key employees (and those moving to new positions) during the initial days of their assignment.

As an example, during a client company [annual revenue at $58 million] planning session with the owner and entire management team present, I was astounded at their approach to a turnover rate in excess of 40 percent per year. The three operating unit managers were asked to discuss their unit’s revenue recognition and turnover rate. To the chagrin of the CEO, one manager did not know the revenue figure for his group, and none of the three, nor the human resources manager, could recite the number of employees lost in the previous year. When management doesn't know, you have uncovered one real cause for problems. You first have to acknowledge that a problem exists, look for the cause(s), then do something — identification alone is not enough.

Are communications ineffective?

Ineffective meetings, management information, or inter departmental coordination can destroy a business from the inside out — even as it is growing.

If all that is accomplished during 'Bull Sessions' is a lot of . . . well, “Bull” . . . then this is clearly the fault of the leader. It's a leader's duty to limit the scope of topics discussed, to establish an agenda — with specific begin/adjourn times — and stick to it. Limit participants too — not everyone needs to be

involved in every topic, what a waste of time and productivity. Demonstrate organization by managing your meetings and your team will demonstrate that organization by managing your company.

What message are you sending? Remember, what is *not* said is often more destructive than what is. Unnatural actions or behavior, such as ‘closed door meetings,’ will most certainly set off the rumor mill. People need to know or they are left to their own imagination — and that is always worse.

Equally important, level with them — then *get the stay versus go* decision. To address the issues in a forthright manner is no guarantee that you will keep everyone, or that everyone will believe what has been said. But not to communicate what is going on is a lack of leadership; so don't be surprised when employees don't do what you want.

Are goals unclear?

Chronic failure to achieve stated business goals suggests a problem far more serious than a lack of performance. Often, it implies a lack of clarity regarding the owner's goals, and usually indicates a failure to secure management team 'buy in'.

Take a long, hard look at the goal setting process. Set goals and hold managers accountable for success.

What is the company's goal? The mission statement should be a directive that states this goal. What usually comes through is "... we are the best at providing a lot to everybody ..." which doesn't say anything. Set a mission statement that tells customers, employees, and stockholders where the company is headed. If it can't be articulated . . . does it really exist? A good mission statement should address six elements, and all six:

- **Service/Product definition —**What do we do or provide?
- **Generic customer need —** Why will they buy?
- **Market definition —** Who will we sell to? Where are they?
- **Technology —** How will we deliver our products and services?
- **Levels of vertical integration —** How much will we do?
- **Distinct competence —** Why will they buy from us?

Most companies are too generic in their definition. Their mission statement is not well thought out. Competition dictates that you focus. Don't underestimate the importance of your key competencies, those strengths that no one else has. Be honest, this doesn't mean just show up at the door. Identify goals that are in sync with these strengths. Do they meet ultimate objectives? If not . . . then why use resources to accomplish them? Remember the ultimate goal . . . companies are in this for the money.

Are compensation and incentive programs yielding unsatisfactory results?

While it seems obvious that programs should clearly and directly reward for successful job performance, it's remarkable that many companies unwittingly set up compensation structures that reward performance altogether different from that outlined in the job description; and from what is expected by the board of directors. A word of warning if this is your practice: Be careful what you pay for — you might just get it.

By contrast, managers who are paid incentives based upon gross margin can be more effective than those paid on gross sales. Why? Because they share the burden of poor performance, they're more likely to take corrective action when faced with substandard performers.

Of all the difficult management chores, this isn't one of them. It does assume that you know what you want to accomplish. This requires planning. What is the proper approach? How are people to make it happen? This requires a great deal of thought. Then for the execution: set rewards for performance to attain the plan, pay for performance when achieved, and don't pay for it if not achieved. Set the directive and the goals . . . THEN . . . set the incentive structure.

Is new business waning?

If so, you are out of touch with the marketplace. High prices, unresponsive proposals, and giving more than is required of you are the typical reason companies lose bids.

Commitment to winning new business is essential to success; so identify targets early on — always keeping a close eye on the customer's special needs. Bid to win, and then manage for profit and growth.

Perception is the key; it has many sides . . . to confuse the competition . . . to comfort the customer . . . to fool ourselves. Remember, a dollar must be a dollar of revenue before it can be classified as any other kind. Management must work this area aggressively . . . develop a "We will do what it takes" attitude toward developing new business.

Are any key client relationships deteriorating?

Determine if a decrease in business from long time customers is due to poor market conditions in their industry — or poor service from your company. If it's you, you're probably no longer meeting the customer's needs. Worse — you may not know.

Manage customer relationships carefully. Customer needs, like your own, change. Assign specific responsibility for nurturing customer relationships to all levels of management —not just to those within the sales force. By all means, get out and talk with the customer. How else will you really know what the customer thinks? Few customers will call to tell you that they are not going to buy your product any more; they just stop writing checks.

This issue is controversial . . . hard to pin down. Its like venturing into the unknown, and people are uncomfortable doing that. Address the real issue of how customers perceive the company and its product (s) relative to competition. Implement a plan to satisfy customers, so that they will want to purchase. Don't be lulled into a false sense of security . . . those customers may not always be there.

Does the company create 'products in search of markets?'

Products developed before market needs are assessed can waste resources and be difficult to sell. It is less expensive to create awareness of a product or service that meets an existing demand, than to develop a new market for existing products or services that doesn't exist.

Identify how your key competencies satisfy customer need and produce benefits. Have your team pretend they are your competition; their task is to identify the strategy that you, the competitor, should pursue. Ask you customers . . . simple but effective.

It is the nature of the engineer to want to create a 'Rembrandt,' something special that meets the needs of all customers. This approach can only add cost to the product, often cost that the customer is not willing to absorb. Keep the 'bells and whistles' to a minimum. If the product(s) is technically oriented, perhaps a modular approach will allow a better fit with various customer profiles, by providing a 'pick and choose' option.

Do financial and management reports cover the wrong information at the wrong level?

Financial and operational reports must be accurate, timely, and pertinent. Too often, management receives only traditional accounting measures of company value, instead of cash flow or new business generated. Also, information is often prepared at the wrong level, making it difficult or impossible for management to know what's going on inside their operations.

Cash flow is the best indicator of business health. Prepare forecasts, and then manage to them. Management should determine performance at each level of the business (i.e. profit center, cost center, cash center), and update often.

Does the operation have a track record of failed expansion plans?

Setbacks drain businesses of cash, time, and morale. When companies fail in one effort, management tends to 'pull in its horns' the next time out. The result? Suppressed hopes for growth or expansion. Efforts fail because of inadequate cash, poor management, lack of thorough market analysis, or improper control systems.

Managers who run independent operations must be adept at problem solving, decision making, team

building, and managerial analysis; skills which are not obvious. Understand why your company is successful in its present marketplace, and try to 'model' those conditions in a new marketplace.

Modeling success can produce growth. The entrepreneur wants it to grow, but *want* alone can only drive the company so far . . . and often into trouble. One is not born to be a manager; you need to cultivate these skills. A Model allows you to depict the new environment without yet being there . . . where mistakes can't impact the real bottom line.

What Have We Learned?

Affecting a turnaround takes an array of skills. When in crisis there is no time for a warm up. To affect rehabilitation, the right leader will know how to make the quick and proper decisions, put a plan into action and keep a talented team moving towards a healthy and more valuable end. Specialists are hired for their management ability, the ability to bring order out of chaos, the ability to marshal resources and maximize value from those diverse resources.

Recognizing trouble requires no hocus-pocus. Likewise, solving trouble's accompanying problems takes no smoke and mirrors. If misery likes company, then trouble loves it; problems can multiply at a frightening speed. Seldom is there only one reason for business troubles; more than likely, you'll discover two or three. The balancing act becomes weighing the risk(s) and taking action versus letting the status quo dictate a troubled course.

One thing's sure: the longer you wait to admit that the company is heading for trouble, the more difficult the resulting problems will be to solve. Getting to the real issues is the catalyst toward change — and recovery.

And that's a much more acceptable risk.

About the Author

John M. Collard, a Certified Turnaround Professional and Chairman of Annapolis, Md.-based Strategic Management Partners Inc., a turnaround management firm specializing in interim executive leadership and investing private equity in underperforming companies. He is past chairman of the Turnaround Management Association and brings 35 years senior operating leadership, $85M asset recovery, 40+ transactions worth $780M, and $80M fund management expertise to advise company boards, institutional and private equity investors, and governments. For more information about Strategic Management Partners, call (410) 263-9100 or log on at ***www.StrategicMgtPartners.com*** or contact us at ***Strategist@aol.com***.

Sections ***Index*** ***Contact***

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Strategic Management Partners has substantial experience advising corporations and individuals on the strategic and mechanical issues of corporate development and governance, operating management and turnarounds for asset recovery. Our principal has over 30 years experience in P/L Management, Strategic Planning and Repositioning, M&A for Strategic Advantage, Finance, Investing, Raising Funds, Sales/Business Development, Building Selling and Marketing Teams, and Operational Auditing = In Public & Private companies = In healthy and crisis situations.

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Sections ***Index*** ***Contact***

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Ste

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Index

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