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Work With Turnaround Professionals to Preserve Value

Annapolis, MD 21403

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Lending & Risk Management News (RMA) published an Article of Interest by John M. Collard, turnaround specialist and equity investor.

Work With Turnaround Professionals to Preserve Value

By John M. Collard

Lenders aren't in the business of closing down companies — nor do they want to be. When a credit becomes financially troubled, lenders often seek an alternative to closing down the business.

A company's financial problems often result from mismanagement. When existing management doesn't possess skills to deal with crisis, a turnaround specialist may be needed.

Most lending institutions send troubled credits to the "work out" department. Make no mistake, this step is usually the first in a long legal process that works the credit out of the bank. The specialist can add value by stabilizing a situation and bringing credibility; thereby making the credit more desirable to the next tier lender with an appetite for more risk.

Foreclosure is painful for lender, borrower, and other stakeholders. At the very least

there will be substantial legal fees, other costs, loan loss reserves, and perhaps a loss of principal. In many cases, it is in everyone's best interest to restore the company to financial health.

Contrasting Leadership Styles

We Compare The Skill in Stable, Healthy Scenario and in the Troubled or Turnaround Situation:

Focus = On Objectives when healthy, but on Survival, Action, Problem-Solving when in trouble

Decision Making = Deliberate when healthy, but Decisive, Immediate when in trouble

Authority = Delegate when healthy and situation allows, but Direct Involvement is key when in trouble

People = Develop skills when time allows, but Recruit Talent, Stress Communications when in trouble

Leader Respected For: Management Reputation when healthy, but instead for Financial Credibility and Decisiveness when in trouble

Leader Known For: Consistency when healthy and stable conditions, but instead for the Ability to Shift Gears when in Trouble and time is of the essence

Leadership Styles

The management skills necessary to rescue a troubled company are dramatically different from those needed to manage operations and growth in a healthy company. In a healthy company, management focuses on long term objectives, coaching, and team building. With the luxury of time, the occasional mistake generally will not do lasting harm. However, in a financially distressed company, time becomes the enemy. As the company's problems compound and cash flow evaporates, it becomes critical for management to act quickly and decisively.

In a turnaround situation, management must focus on short-term survival. While a manager in a stable environment should be known among employees and shareholders for consistency in making decisions, a manager in a troubled company must be able to shift gears to deal with the daily crises that inevitably occur.

Existing management often goes through a "denial" phase. They tend to blame their situation on external factors, such as the lender's refusal to advance additional funds, rather than examining the way the company is managed. In the eyes of management, the lender becomes an enemy. If a negative view of the lender's role develops, the lender may need leverage (a condition of added financing, or threat of foreclosure) to

recommend use of an outside advisor.

Lender Liability

Lenders should avoid deciding on which turnaround professional the borrower should use. Lenders can insist on the use of a turnaround specialist, perhaps as a condition of additional capital. Many lenders present the borrower with a "short list" of specialists; however, the company should be free to choose its own advisor or leader. By recommending a particular professional, the lender may expose the bank to liability.

Finding the Right Turnaround Professional

Turnaround specialists generally are either interim managers or consultants. Interim managers will replace the CEO, take the decision-making reins, and guide the company through troubled waters, hopefully to safety. Consultants advise management; possibly the same management that got the company into trouble in the first place. Whether a consultant is effective depends on management's willingness to listen and to implement the specialist's recommendations.

The turnaround specialist must possess the skills to deal with a financially troubled company and have the ability to make the tough decisions needed during a recovery. 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. If the company requires special expertise, then the specialist will attract that expertise. Remember, experience in dealing with crises and change may be more important than industry experience.

It is important that the turnaround professional be financially credible and honor commitments. The company, bank and other interested parties should be able to rely on the specialist to protect their interests while providing them with accurate information they need on a timely basis. The earlier trouble is detected, the more probability of turnaround success. When hiring a turnaround specialist:

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

How the Specialist Operates

The specialist offers a new set of eyes, skills and understanding of troubled situations to independently evaluate the company's circumstances. The process will focus on several issues:

- * Is the business viable?
- * What is the purpose of the business?
- * Should it be saved? Why? Are those reasons valid?

- * Is there a core business which can be the source for the emerging business?
- * Are there sufficient cash resources to fuel the recovery?
- * Which existing managers are capable of leading parts of the company?

Remember, not all companies are salvageable.

This fact-finding must occur 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. Analyzing 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 will be prepared. 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.

The Turnaround Management Association (TMA), based in Chicago (www.turnaround.org), can be one source for professionals. TMA has developed a Certified Turnaround Professional (CTP) program (www.actp.org) to help the selection process. TMA also offers loan officers a training forum to learn more about the benefits derived from working with turnaround specialists.

A good turnaround specialist will develop a permanent management team within the company to preserve value, instead of hiring a large team of outsiders who, when they leave, take that value with them. The specialist should work themselves out of a job to be most effective, while leaving the company with the ability to grow and prosper as a stand alone going concern.

For more information about working with turnaround professionals, visit: www.StrategicMgtPartners.com or call (410) 263-9100

About the Author

John M. Collard, is Chairman of Annapolis, Maryland-based Strategic Management Partners, Inc. (410-263-9100, www.StrategicMgtPartners.com), a nationally recognized turnaround management firm specializing in interim executive leadership, asset recovery, and investing in underperforming companies. He is Past Chairman of the Turnaround Management Association, a Certified Turnaround Professional, and brings 35 years senior operating leadership, \$85M asset recovery, 40+ transactions worth \$780M+, and \$80M fund management expertise to run troubled companies, and advise company boards, litigators, institutional and private equity investors.

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