


Turnarounds & Crisis Management

Solutions to Complex Business Problems

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Turnaround and Crisis Management

Course Objectives:

1. Timing of Hiring a Turnaround Management Firm
2. Factors Causing Companies Delays in Retaining a Turnaround Firm
3. Obstacles in Retaining a Turnaround Manager
4. Criteria Considerations for Engaging a Turnaround Manager
5. Evaluations of Turnaround Experts
6. Compensation Models by Turnaround Firms
7. Interaction Between Turnaround Professionals and the Bankruptcy Attorney
8. Reasons for an Unsuccessful Turnaround

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Timing of Hiring a Turnaround Management Firm

- Nature of Turnaround Situation
 - Declining business
 - Substantial or continuing losses
 - Danger of failure
- Preliminary Viability Analysis
 - Identify viable business unit.
 - Determine availability of interim financing
 - Determine adequacy of organizational resources

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Timing of Hiring a Turnaround Management Firm

- Existence of Crisis Management Issues
 - Unstable situation regarding
 - No cash flow or bank borrowing availability
 - Vendors cease shipping except on COD basis
 - Customer shipments are disruptively late
 - Disruption in manufacturing
 - Comparative Market Values
 - Significant decrease in market value of securities, value of the company, or assets
 - Real estate
 - Businesses -- recently sold

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Timing of Hiring a Turnaround Management Firm

- Going Concern Value Issues
 - Revenue Multiple
 - Service industries
 - Different multiples for different revenues
 - Discounted Cash Flow
 - Capitalization of Earnings or Cash Flow (EBITDA)
- Business Failures
 - Objectives
 - Identify causes
 - Identify stages
 - Describe how to detect failure tendencies
 - Must look for underlying cause not symptoms

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Timing of Hiring a Turnaround Management Firm

- Poor Management
 - Failure to keep pace with changes in the market place
 - Lack of operating controls
 - Over-expansion and Failed acquisitions
 - Excessive leverage and debt
 - Lack of management depth
 - Inbred bureaucratic management

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Company Delays in Retaining a Turnaround Firm

- Detailed Viability Analysis by Company -- Strengths and Weaknesses
 - Organizational Structure
 - Market Capability
 - Production Capabilities
 - Engineering and Research and Development
 - Administration
 - Peer Group Analysis


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Company Delays in Retaining a Turnaround Firm

- Detailed Viability Analysis by Company-- Environment and Competitive Ability
 - Competitive Ability
 - Threat of new entrants
 - Threat of substitute products
 - Bargaining power of buyers
 - Bargaining power of suppliers
 - Rivalry among current competitors


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Company Delays in Retaining a Turnaround Firm

- Bank Group Management – In a Workout Environment
 - Existing Sr. Secured Lender ("lenders") Perspective
 - Communication with lenders
 - Proactively manage communication with the Bank Group
 - Discussions regarding the activities of counsel and intent to engage financial advisors
 - Timely updates on status of financial results and operating issues
 - Provide adequate time for lenders to respond
 - Pre-selling difficult requests to Sr. secured lender agents
 - Need a process to deal and negotiate with the lenders


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Company Delays in Retaining a Turnaround Firm

- Bank Group Management – In a Workout Environment (Continued)
 - Role of the Agent
 - Organize the Bank Group
 - Agent's Balancing Act
 - Lead the bank group but don't get too far out in front
 - Selection of counsel and financial advisor
 - Analysis of liquidity / business viability
 - Evaluation of options
 - Communication
 - Determine lender positions as agent communicate with Borrower's management and other Stakeholders


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Obstacles in Retaining a Turnaround Firm

- Does the Borrower need a professional crisis manager?
 - In most turnaround situations top management is replaced
 - Change in leadership often required to change existing mindsets
- Defining the role of the crisis manager
 - Interim CEO, CFO or CRO / Responsible Officer
 - Financial Advisor
- Liquidation Values
 - Forced sale v. orderly liquidation
 - Deduct administrative expenses related to possible liquidation

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Obstacles in Retaining a Turnaround Firm

- Understanding differences between Turnaround and Restructuring
 - Turnaround -- solving operating problems in all business areas
 - Restructuring -- developing a financial structure for a basis for the turnaround
- Understanding Restructuring Alternatives
 - Should the business liquidate or reorganize?
 - Chapter 7 or Chapter 11 Liquidation or Chapter 11 reorganization
 - Should the action be taken out of court or in bankruptcy?
 - Considerations: cash, profitability, debt structure, business segment closures, balance sheet, collateral, debt/equity.

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Obstacles in Retaining a Turnaround Firm

- Overall Viability Assessment by Company
 - Industry in which the debtor operates
 - Debtor's position in the industry
 - Debtor's management awareness of issues
 - Debtor's cost structure
 - Debtor's debt structure
 - Debtor's capital structure

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Criteria Considerations for Engaging a Turnaround Firm

- Overall
 - Management of Cash
 - Ability in turning the business around.
 - Provide direction for turnaround and reorganization engagements.
 - Identify opportunities to render valuable services in turnarounds & reorganizations
 - Understand impact of Bankruptcy Code - Out of court and bankruptcy cases

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Criteria Considerations for Engaging a Turnaround Firm

- Financial Advisors Expertise as to Parties to be served
 - Debtor, DIP, or Trustee
 - Senior secured lender
 - Unsecured creditors committee
 - Bonds & other creditors' committee
 - Equity holders' committee
 - Individual creditor or shareholder
 - Examiner or retained by examiner (rare)
 - Trustee

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Criteria Considerations for Engaging a Turnaround Firm

- Stages of Business Failure
 - Business growth or shrinkage
 - Cash Shortage
 - Financial Insolvency – difficult determining
 - Total Insolvency
- Incubation Period
 - Industry: start-up, early, growth, & mature
 - Change in product demand & commodity
 - Increase in overhead costs.
 - Obsolete production methods.
 - Increase in competition.
 - Insufficient Information to Manage Sales, GM, & Expenses

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Criteria Considerations for Engaging a Turnaround Firm


- Cause of Business Failure
 - Growth, debt, systems, & acquisition return
 - External
 - Economic change
 - Competitive change
 - Government constraints
 - Social change
 - Technological change
 - Management and Internal
 - Fraud

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Criteria Considerations for Engaging a Turnaround Firm

- Turnaround Management Factors Which Determining the Success of a Plan
 - Management willingness to recognize the magnitude of the problem
 - Management willingness to recognize the need specific help and they are in a crisis situation
 - Management willingness to change
 - Extent to which early action is taken to stop the negative cash flow
 - Willingness of Senior Secured Lenders
 - Finding a viable part of the business
 - Quality and Honesty of management
 - Attitude of the unsecured creditors', customers, and lenders


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Criteria Considerations for Engaging a Turnaround Firm

- Direct stages of turnaround process
 - 1. Management change
 - 2. Situation analysis
 - 3. Selection and design of turnaround strategy
 - 4. Emergency action.
 - 5. Restructuring and profitability enhancement
 - 6. Return to normal


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Criteria Considerations for Engaging a Turnaround Firm

- Factors Determining Success of a Plan
 - Engage experienced crisis management professionals
 - Crisis Manager assumes management of cash
 - 13-week cash budget—develop positive cash flow
 - Development of a viable business plan
 - Relationship with Senior Secured Lender and their willingness to negotiate a workout
 - Prospect of DIP & post confirmation financing

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Criteria Considerations for Engaging a Turnaround Firm

- Types of Turnaround Strategies -- Operating
 - Revenue Increasing Strategies
 - Cost Reduction Strategies
 - Asset Reduction and Redeployment Strategies
 - Competitive Repositioning Strategies
 - Combination Strategies
- Objectives
 - Take actions necessary to enable the organization to survive
 - Establish positive operating cash flow
 - Raise cash to implement strategy
 - Protect and develop resource needed for future profitability and growth

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Criteria Considerations for Engaging a Turnaround Firm

- Operational efficiency
 - Successful firms concentrate on efficiency first, products second, and then on marketing and sales
 - Display production efficiencies to employees daily, weekly, & monthly
 - Establish efficiency improvement measurements and reward employees for successful improvements.
 - Successful companies reduce cost relative to present revenue levels. Unsuccessful companies attempt to increase revenue to cover existing costs.
 - Successful companies implement proven efficiencies immediately--but work through people

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Evaluation of Turnaround Experts

- Have Turnaround Manager Define Objective
 - Explain a strategy to turn the business around
 - Define key corporate and business strategies
 - Define specific goals and objectives strategy
 - Describe the framework for integration of goals and objective strategy into business plan
 - Describe functional action plans

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Evaluation of Turnaround Experts

- Discuss the Turnaround Managers Selection of Alternatives to Issues:
 - Describe alternatives available to solve business problems
 - Define criteria that should be considered in evaluation alternatives
 - Describe a preplanning plan
 - Explain the type of services the financial advisors may render

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Evaluation of Turnaround Experts

- Evaluate their ability to explain and obtain objectives to:
 - Determine Value of the business
 - Assists in formulating a plan
 - Assist in finding sources of credit.
 - Describe the process of recovery
 - Explain the stages of the recovery
 - Identify some techniques that might be used in turning a business turnaround

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Evaluation of Turnaround Experts

- Describe Their Operations Management Successes as to their:
 - Survival rate of companies continuing operations
 - Successes in communication with suppliers, buyers and employee representatives are important
 - Successes in review of purchasing procedures including identifying extra charges and pricing problems
 - Ability to identify vendor and supply problems including an identification of critical vendors and alternate suppliers

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Evaluation of Turnaround Experts

- Evaluate the Turnaround Manager Cash Management Process and Achievements
 - Describe their development of a cash management system for operations.
 - Development of COD procedures for Critical Vendors
 - Replace all Non-Critical Vendors
 - Their opinion as to a 13-Week and/or 12-Month Cash Flow Analysis
 - Reporting actual to forecasted results
 - Daily reporting and analysis of cash balances

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Evaluation of Turnaround Experts

- Evaluate the Turnaround Managers Ability to:
 - Assist the debtor in analyzing operational problems, designing a turnaround strategy and implementing the strategy.
 - Perform consulting activities to assist the debtor in making decisions, development of a business plan, etc.
 - Assists the debtor -- the type of action to take to resolve its financial problems.

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Evaluation of Turnaround Experts

- Evaluate the Turnaround Managers Ability to Evaluate Turnaround Techniques:
 - Business Turnaround Techniques
 - Just-in-time (JIT)
 - Eliminate activities that do not add value
 - Commitment to a high level of quality
 - Commitment to continuous improve efficiency of an activity
 - Emphasize simplification/increased visibility to identify activities not adding value

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Evaluation of Turnaround Experts

- Evaluate the Turnaround Managers Ability to Access Manufacturing Processes:
 - Activity Based Costing Analysis
 - **Step 1**
 - Trace cost according to their activity
 - Divide costs into homogeneous pools
 - Determine appropriate cost driver
 - Example

Activity	Driver
Materials handling	# of components
Set-up	# of hours
Packing/shipping	# of orders
 - **Step 2**
 - Calculate a rate for the cost driver
 - Apply the cost to the product

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Evaluation of Turnaround Experts

- Evaluate the Turnaround Managers Ability to Assess Retail Businesses:
 - **Four Wall Analysis for Retailers**
 - Problems common among retailers
 - Overview of four wall analysis
 - Sales
 - Expenses: Direct; Assignable; Allocable
 - Treatment of expense allocation
 - Contribution margin information
 - Rank stores
 - Establish performance thresholds
 - Non-quantitative considerations

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Evaluation of Turnaround Experts

- Discuss their Management Change Objectives and How they would:
 - Access that "cash deficit bleeding" can be stopped and the business is viable
 - Select the top management team that will lead the turnaround
 - Replace management and board members that will hinder the turnaround effort
 - Identify the appropriate turnaround strategy
 - Develop a preliminary action plan

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Evaluation of Turnaround Experts

- Operational efficiency
 - Successful firms concentrate on efficiency first, products second, and then on marketing and sales
 - Successful companies reduce cost relative to present revenue levels. Unsuccessful companies attempt to increase revenue to cover existing costs.
 - Successful companies implement proven efficiencies immediately--but work through people
- Changing the Culture
 - Challenging and changing the status quo
 - Rewarding those who change
 - Terminating those who do not adjust to changing needs

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Evaluation of Turnaround Experts

- Manufacturing/Operations Management
 - Eliminate unprofitable operations
 - Reduce the work force
 - Reduce inventories
 - Control purchases
 - Increasing productivity

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Evaluation of Turnaround Experts

- Marketing Management
 - Reassessing product line and competitive pricing practices
 - Exploiting existing products and developing new products
 - Improving the customers and distribution mix
 - Improving sales and marketing productivity and effectiveness
 - Improving profit per customer
 - Correcting serious pricing problems
 - Product line pruning
 - Weeding out weak customers and distributors
 - Getting sales and marketing costs in line with industry averages

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Evaluation of Turnaround Experts

- Turnaround Manager ability to affect Manufacturing/Operations Management
 - Eliminate unprofitable operations
 - Reduce the work force
 - Reduce inventories
 - Control purchases
 - Increasing productivity

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Compensation Models by Turnaround Firms

- Debtor, DIP, or Trustee Parties to be served
 - Hourly rates ranges by positions experience by individual
 - Hourly rates ranges by positions experience by individual plus success fee for exiting bankruptcy, timing of exit, and obtaining exit financing.
 - Fixed monthly fee primarily for management positions assumed by Turnaround professionals such as CRO, CEO, COO, CFO, Treasurer, Controller, and other. May also include a success fee.
 - Firms representing entities in bankruptcy must have consistent rates for all clients but may be hourly or fixed at the same rate for each level of experience.

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Turnaround Professionals and Bankruptcy Attorneys Interaction


- Areas of responsibility
 - Turnaround Managers (Financial Advisors) are responsible for the business and financial aspects of the business and document negotiations.
 - Provides the debtor's counsel--information needed to prepare the schedules, statement of affairs, etc. to file a petition
 - Prepares special financial statements--e.g., balance sheet as of the petition date
 - Workout Professionals can help calm down the bank group participants
 - Workout Professional benefits from the help of the relationship officer (e.g. company history, business, other issues)

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Turnaround Professionals and Bankruptcy Attorneys Interaction

- Turnaround Professional Financial Reporting in Bankruptcy (Preliminary)
 - Set up new asset accounts for selected items such as inventory and accounts receivable that might be pledged
 - Claims processing plan
 - Compliance reporting for DIP financial agreement
 - Filing date selection--avoid a separate closing if filing date is near month end or even better if at or near end of quarter or fiscal year.


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Reasons for an Unsuccessful Turnaround

- Primary Objectives Not Met Timely
 - Enhance profitability through effective and efficient management of current operations
 - Reconstruct the business for increased profitability, return on assets and return on equity
- Financial Management Objectives Not Met Timely
 - Improving Liquidity
 - Restructuring the balance sheet
 - Developing control systems
 - Creating a managerial accounting systems that reflects the costs of products manufactured and provides relevant data to management to guide in product selection.


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Reasons for an Unsuccessful Turnaround

- Manufacturing/Operations Management Not Met Timely
 - Developing on-going productivity improvement programs
 - Developing cost system, as noted above, to follow cost causes, such as ABC
 - Conducting overhead value analysis periodically
 - Establishing on-going profit improvement programs
- Lack of Sufficient Culture Improvements
 - Improving the people mix of the business
 - Restructuring the organization for competitive effectiveness
 - Developing reward and compensation systems that reinforce the turnaround efforts and that are based on shareholder value


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Reasons for an Unsuccessful Turnaround

- Failure to Improve Financial Management
 - Development of strategic accounting and control systems that provides timely and relevant information in both conventional and nonconventional formats, especially relating to cost of products or services.
 - Maintenance of the tight financial disciplines that were learned during the turnaround process.
 - Restructure the business's long-term financing to maximize shareholder value.


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Reasons for an Unsuccessful Turnaround

- Engineering and Research and Development Failures
 - Unable to achieve lower cost through product design
 - Failure to establish advanced technology monitoring systems
 - Unsuccessful strategic leverage in all engineering and research and development activities
 - Unable to seek ways to avoid complacency

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Restructuring Profit Advisors, LLC

Restructuring Profit Advisors, LLC specializes in providing in-depth financial and operational analysis and value added creative solutions to stakeholders in distressed situations.

- We provide strategic advice and analytical services to debtors or stakeholders of companies experiencing liquidity problems and other issues that typically face a business in transition.
- Our understanding of the perspective of company and creditors enables us to quickly assess key issues and design strategies driven to a timely and viable solution.
- We work in small teams comprised of highly experienced professionals. We understand how to quickly gather and analyze the information necessary for decision making. Our targeted approach and effective case management enable us to quickly assess key business drivers and identify viable strategic alternatives available to all parties in interest.
- Our corporate recovery and restructuring services primarily focus on:
 - Turnaround and restructuring
 - Bankruptcy process and execution
 - Crisis management
 - Transaction advisory and due diligence
 - Sourcing interim and replacement financing

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