

REPRINTED FROM  
THE JOURNAL OF CORPORATE  
RENEWAL

# Seven Tactics for Restructuring in a Turbulent Financial Market

By Walt M. Denekas, CTP, Managing Director, Carl Marks Advisory Group

**R**estructuring troubled businesses typically involves some form of financial restructuring: changing the mix of equity and debt, renegotiating loans, or finding one lender to take over another. The meltdown in the U.S. banking system and the widespread lack of confidence in global financial markets has radically changed the available options for turnaround professionals to conduct successful restructurings.

Debt, equity, and commercial paper of companies in financial distress are no longer labeled “high-yield” or even “junk,” but are now tagged “toxic assets.” Even getting debtor-in-possession (DIP) financing to support a bankruptcy is difficult in today’s challenged market. The result has been an increasing number of companies going directly from bankruptcy into sale or liquidation and a sharp reduction in the willingness to do financial and operational restructurings, even if they could result in significantly greater enterprise value.

Given all that, a logical question is: Is it possible to do an operational turnaround in such a hostile business climate at all? The answer is yes. Companies have completed successful turnarounds without new financing, but doing so requires skill, a certain amount of luck, and a plan that management believes it can execute.

What follows are seven tactics learned from successful turnarounds in which managers knew from the outset that no new significant amount of capital was available.



**1 Adopt the mindset that funding is unavailable from any outside source, except perhaps from stakeholders with a significant amount to lose.**

Even then, one should expect such funding to be minimal and provided reluctantly. Turnaround professionals facing such situations should think of themselves as military commanders in hostile territory who know that they have no options for obtaining reinforcements or retreating; they must fight their way out on their own. Such commanders focus on shoring up defenses, conserving food and ammunition, and plotting clever counterattacks that can be

executed with limited resources. In this situation, survival today takes priority over a victory tomorrow.



**2 Lock in existing financial resources.**

If loans that are being reasonably well-serviced are in place, a turnaround professional should consider extending them before the end of their terms. Renegotiating an existing loan will likely result in a higher interest rate and tighter covenants, but it may be easier for the bank to amend an existing loan today than to roll it over into a new one later. A turnaround professional should share the plan with the lenders so that they know they are not expected to increase their risk on the company’s behalf.



**3 Plan in multiple time frames.**

A 13-week cash flow forecast is a basic requirement, but forecasts that extend at least through the peak seasonal funding requirement also are needed. This helps set restructuring targets to provide adequate liquidity and timelines to implement them to be used as a budget that the turnaround professional and lenders can reference to track performance.

At the same time, since cash flow needs are usually committed by events occurring within 30 to 60 days or even earlier, the turnaround professional must start managing some short-term metrics. Is the order rate this week sufficient to support the sales plan for next week? Are the shipments today sufficient to support the downstream collection forecast? Previewing an accounts payable check run is important, but incoming inventory also must be regulated to stay within the downstream disbursement budget later. If the upstream metrics go off track and aren’t detected, the 13-week forecast can quickly become unattainable.



**4 Make inventory the company’s piggy bank.**

Here are five specific places to start: excess/obsolete inventory, material usage and yield, minimum order quantities, safety stock, and shortening the procurement cycle.

► See page 2

## SEVEN TACTICS FOR RESTRUCTURING

from page 1

Admittedly, now is a particularly difficult time to unload excess and obsolete inventory, as liquidation channels are overflowing with excess goods. It may be more financially viable to rework products into saleable forms than to liquidate them at today's prices. Excess inventory can be used for promotions, for example, by offering consumers a discontinued but otherwise first-quality product in lieu of a cash rebate.

When JenOmex, a Mexican border mini-blind plant, created a virtual "corral" around its plastic inventory, it discovered that worn production dies were extruding parts that were 50 to 100 percent thicker than specification. The \$3 million the company saved from repairing the dies covered more than half of its restructuring cost reduction target.

Minimum quantities from suppliers should be renegotiated. It's better to pay a slightly higher unit cost for products that can be sold right away rather than to pay for labor, material, and freight on inventory that may be liquidated, destroyed, or held for long periods.

Most companies carry too much safety stock. If safety stocks are set as a percentage of monthly usage, inventory dollars are being wasted on the most accurately predictable and/or most frequently ordered stock keeping units (SKUs). If a company can cover demand fluctuation on a popular SKU by moving the next production order up or back, it should not carry a lot of safety stock on it.

Finally, one Illinois manufacturer eliminated 95 percent of its finished goods inventory by telescoping its production cycle into two days shorter than its published lead time. Except for rush orders filled from a small "ambulance stock," all shipments were made to order, providing nearly 100 percent on-time delivery and 100 percent line fill.

**Cut costs even if it's risky.**

In a self-funded turnaround, it is okay to mortgage the future; otherwise,

there may be no future at all. Paradoxically, while customers are themselves downsizing, they are demanding better service from their suppliers. As a guide, one should look hardest for cuts in departments that have the least customer contact. Cutting the finance department may be preferable to downsizing the customer support staff too far, for example. With survival at stake, it is preferable to err on the side of cutting too far. A company can always hire back, and in a tight job market, it often can rehire the best of the people who were terminated.

**Open informal communication lines.**

Good communication is a cliché, but this moves to another level entirely. If workers are represented by a union, this is the time to find out whether it will support or oppose a restructuring and to try to bring union members under the tent. This is not the time for memos, marathon negotiating sessions, or lengthy e-mail exchanges. Restructuring professionals should take a lesson from the world of sports. In football, a short huddle precedes nearly every play. It lasts about 30 seconds, sets the direction for the play, and ensures that everyone gets the same message at once. A turnaround professional's communication with the organization needs to be similar: fast, effective and, as much as possible, face-to-face.

**Take a hard look at product development.**

Although cash is the lifeblood of a company, new or improved products offer evidence of its intention to stay in business and give its customers a reason to meet with its salespeople. In a self-funded turnaround, though, one must find ways to develop new products more effectively.

Companies selling everything from dishes to military aircraft have discovered that small, focused teams can do a great job coming up with new products and often do it faster.

Lockheed Martin's Skunk Works is perhaps the best-known example, but there are many others. Such groups are established within organizations and given high degrees of autonomy, unhampered by bureaucracy.

Bernzomatic Corporation, then a small blowtorch manufacturer that had little cash, needed an oxygen-propane torch for the do-it-yourself (DIY) market. With no money for tooling, the production models were made using off-the-shelf fire extinguisher holders and bicycle handlebar grips. The new product quickly dominated the DIY oxy/propane market and is still sold, in an upgraded form, at most home center stores. That's product development on a survival budget!

**No Magic Bullet**

Will these tactics always work? No. A corporate turnaround isn't a cookbook process in any circumstance, let alone when financial restructuring opportunities are all but nonexistent. This approach should be taken only if there's an executable plan behind it.

On the other hand, a successful turnaround usually creates more value than can be realized through liquidation or a sale under U.S. Bankruptcy Code Section 363. For management teams that have pulled it off, doing a turnaround with only their own resources often marks the most satisfying period of their careers. For turnaround professionals, doing so needs to be a high-choice strategy in their personal playbooks. •

Walter M. Denekas, CTP, is a managing director with Carl Marks Advisory Group LLC.

He has been a manager in 27 restructuring engagements, including some of those mentioned in this article. Denekas is a member of TMA's New Jersey Chapter.



This article is reprinted with permission of the *Journal of Corporate Renewal*. All rights reserved.