The Most Important Turnaround Lessons I Ever Learned

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I consider myself to be very fortunate. Early in my career, I had the privilege of attending the Johnson Graduate School of Management at Cornell University, which I feel is one of the finest business schools. It was tough but I paid attention and learned a lot. However, there are some situations that even the best education cannot provide adequate preparation.

Some of my best lessons have been on the job and in the trenches. Sometimes these lessons resulted from trial and error; at times, they were painful and disappointing. In other situations I was fortunate to have been working alongside someone with more experience and I learned by watching and doing.

A few of these topics may be obvious and familiar to you, while others less familiar. However, don't let the brevity or simplicity of these pearls of wisdom distract from their importance. I have been involved in some of the largest restructurings in history and in some of the toughest turnaround situations and, in each case, these lessons have been consistently used to achieve aggressive and challenging turnaround and restructuring objectives.

These tidbits of advice are not likely to be found in a college textbook, may lack structure and are not rooted in academic research. Consider this a fly-on-the-wall of 25 years of turning around companies and improving business performance. Take what you can from them, add them to your arsenal of management tools and keep learning – always keep learning.

Cash is King

This is a common phrase and a well-known turnaround imperative. Yet, I am frequently amazed how few CEOs and senior managers realize that cash trumps all else. Nothing is more important than cash flow – not sales, not customers, not suppliers, not employees – without cash the company will have none of these. The primary and paramount objective in any turnaround, in any company, in any distressed situation is to increase free cash flow and become cash-positive.

This is where specialized professionals earn their weight in gold. Like anything else, increasing free cash flow and doing it with lightning speed is a skill. The success of any turnaround and the survival of the company will largely rest on how much cash can be generated in the shortest possible time. This often requires tough decisions, with little analytical due diligence, that can have dramatic consequences on the normal operations of a companies. Turnaround and restructuring professionals make huge, enterprise-changing decisions almost as easily as most CEOs order their lunch. However, the survival of the company is in the balance and speed of execution is essential.

Cash is king; it trumps all else. And as the saying goes: *Out of cash – out of time – out of business!*

Establish Credibility with Lenders and Creditors

Believe it or not, your lender or bank understands your situation better than you may think. Experiencing financial difficulty may be a new or at least a rare event for a distressed company but your lender likely has been through the very same process with dozens or even hundreds of other companies. They get it. Be straight with them and don't try to hide the realities of your situation; they will discover all the facts eventually. Work constructively with your lenders; understand their situation, their needs and negotiate with their objectives in mind.

The fastest way to establish credibility with lenders and creditors is to properly manage expectations. The opposite is true as well; failing to deliver on a commitment is a credibility killer. Early in the turnaround and restructuring process implement this simple directive: *Do what you say, say what you do and never over promise.*

Establish Priorities

In turnarounds, the *80/20 rule* rules. Named after an Italian economist, the 80/20 rule or the Pareto Principle predicts that 80% of the effects are the result of 20% of the causes. I don't know exactly why but it's actually based on mathematical distribution theory. All I know is – it works! For example: 80% of sales come from 20% of the customers; 80% of profits come from 20% of the products; 80% of the waste comes from 20% of the work and so on. This is an extremely important principle in a turnaround or distressed situation.

Don't focus on everything, don't try to solve all of the problems and don't expect complete results. Look for that 20% - focus exclusively on that. Focus on *that* 20% of customers; improve *that* 20% of products; redesign *that* 20% of work. Turnarounds are a never-ending process of triage, where you need to continually peel back the onion. Look for the drivers – the levers – that critical and pivotal 20%; fix those areas and watch the company improve faster than anyone would have imagined.

Fool's Gold: Increasing Sales and Profitless Prosperity

Sales revenue is NOT cash and, in a turnaround situation, it's all about cash. This may seem like an obvious over-simplification but, in my experience, nearly all CEOs just don't get this. Isolated sales goals are dangerous and misguided initiatives. Although one of the most commonly stated corporate goals, sales growth alone rarely creates increased value in a turnaround or restructuring environment. A directed focus on gross margin dollars and free cash flow are better benchmarks on which to build enterprise value.

Profitless prosperity is a term used by many turnaround professionals to describe a company's mistaken belief that selling more at a lower price or with more liberal terms will somehow save the company. Nothing could be further from the truth. Selling more at lower margins and offering extended payment terms to customers can drain valuable cash in the form of working capital and can actually work against the critical turnaround initiatives.

Sales revenue or cash: when in doubt, which is more important? On the next payroll try paying your employees with 'sales revenue' and watch what happens!

Manage Communications

Feel free to group this one with 'Establish Credibility' but it's so important, it deserves notation. Underperforming and distressed companies are often devoid of any kind of communication strategy and quickly become breeding grounds for the rumor mill. Rumors, false information and damaged company reputations are the result of poor or lack of communication management.

Once a company gets into trouble, the management team becomes secretive and reserved about the company's situation and what needs to happen in order to recover. This directly leads to people, within the company

> *"Prioritize everything, master the 80/20 rule, then sit back and watch everyone ooh and aah!"*
> – *Carter Pennington*

as well as customers and vendors, to draw their own conclusions and spread their own opinions disguised as facts. Rumors, gossip and hearsay are the result of lack of communication. If you want to keep aspects of your business confidential – communicate!

It's counter intuitive but true. A turnaround manager must openly discuss the company's situation with lenders, customers, vendors, the media and most importantly, the employees.

This doesn't mean you hang out the company's dirty underwear or give out trade secrets; it also doesn't mean that all parties get the same level of detail. However, all constituencies and stakeholders must be given accurate and regular updates on what's going on, what's broken within the company, how it will be fixed, when will things be ok and how the company is progressing.

The choice is simple: either the company manages the communication or the rumors and gossip will manage the company.

Build from a Strategy

With a firm name of Cardinal Strategy Group, it should come as no surprise that I'm big on strategic planning – a silly name for a firm if I weren't! The fact is, developing a robust and innovative strategic plan is often overlooked in many turnarounds. Distressed companies often have a narrow and short-term planning horizon and usually have been in a survival mode for months, and in some cases years. Strategic planning often takes the back seat to tactical and short-term planning. However, once the turnaround process passes the crisis management stage, it is vitally important that strategy moves up to the front seat.

A good strategic plan should be built from the customer and market perspective and clearly demonstrate, with detailed initiatives and accountability, how the company will change and work toward creating competitive advantage. Very few managers and equally fewer turnaround professionals have the formal training that is required to develop a solid strategic plan. It would be wise to retain a specialist to help navigate that process and assist with changing the culture of the company to embrace the new strategic direction. Without a well-thought out and professionally developed strategic plan, the company will be sailing aimlessly, without any real long-term direction.

Trust Your Gut Instincts

Your first impressions are often correct. There are scientific reasons for this. People have far greater perception of situations than their conscious minds reflect. We all absorb significant and voluminous information subconsciously and, along with our individual life experience, develop feelings, opinions and judgments as a result. This is valuable in business and absolutely priceless in a turnaround situation.

Most underperforming and distressed companies have less than perfect information, outdated reporting systems and limited market intelligence. While you need to collect as much information as possible and validate every assumption you make, it often comes down to making a decision, sometimes a really BIG decision, with less factual support than you would like.

Time is of the essence and the luxury of delaying the decision or kicking the can down to some "committee" is just not in the cards. You need to have the confidence to make a really tough decision from your gut and rely on your feelings and personal judgment.

If it smells like a bad idea – stand clear; if your instincts tell you it's a winner – go for it!

At the End of the Day – It's All About People

Another very obvious principle yet it never ceases to amaze me how few CEOs and turnaround managers get this. The simple fact is: you can't turnaround a company – you can only turnaround people. Unless a business is run by a bunch of robots, people are responsible for doing all of the work: making the products, performing the services, dealing with customers, buying from vendors, etc. An underperforming or distressed company usually needs to negotiate with stakeholders, analyze its business, develop new plans, implement new processes and function like an inter-connected living organism.

The turnaround manger needs to create an environment that allows people to be motivated; people need to embrace change and want to make things better. Everyone needs to have the same set of business values and an alignment of goals and objectives. Managers and rank-and-file employees need to be brought into the process as early as possible, contribute to the new changes and have *buy-in*. A successful turnaround manger is a successful manager of people and a leader who shares the same vision, confidence and attitude of the organization. Troubled companies typically have broken organizations, structurally and socially. Fix the organization and the company will fix itself.

While I might get into trouble for saying this, it can't be ignored: no doubt an outstanding starship science officer but Mr. Spock would make a terrible turnaround manager!

Rely on Professionals

Attempting to lead a turnaround or a restructuring without the relevant experience is an invitation to disaster. It's not much different than asking your neighbor for help when you require heart surgery. Your neighbor may be honest, trustworthy, intelligent and he may know you very well – would that be ok with you? Not likely! You would want the best cardiac surgeon you can find. Professionals that specialize in troubled and distressed companies are familiar with your situation; they have been down that road many times. They can make the right decisions, make them at the incredible speed in which they need to be made and will be accountable for their results.

In most turnaround and restructuring situations, many professionals are needed; no single professional has all the answers. The professional turnaround team might include a Chief Restructuring Officer or turnaround leader, bankruptcy attorney, investment banker, operations consultant, real estate broker, media consultant, accounting firm and IT specialist. The specific situation will determine which professionals are needed. Retaining such professionals will be costly but could be the most important and critical investment the company will ever make.

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Bonus Lesson: (one of my secrets)

Leave Your Ego at the Door. Why?? Because nobody else does!! It gives you a competitive edge and the upper-hand when dealing with angry creditors, disgruntled employees, nervous customers, pissed-off vendors and a wide range of other emotionally charged stakeholders. Trust me on this one!