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LEADERS & SUCCESS

# How To Spot Signs Of Corporate Trouble

## Turnaround Experts Cite Erosion Of Cash Flow, Product Sales Drop, Quarterly Losses

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Abe's his name and trouble is his game. Abraham E. Getzler, president of the New York-based consulting firm bearing his name, makes his living cleaning up messes left by others.

Getzler specializes in crisis or turnaround management and usually is brought on board by bankers who have lost confidence in existing management's ability to pilot the company out of troubled waters.

"While some crisis situations may hit a company totally without warning, usually there are classic signals that present management either failed to recognize or just plain refused to accept," Getzler points out.

Failure to meet sales goals ranks as one of the first warning signals that management tends to discount. Companies rationalize such failures in many ways: It's a temporary situation while customers work off inventory levels; it's probably due to this period's sales cutoff date; the sales forecast should be accurate for the year as a whole; and several major new customers are ready to place orders.

Management's denial compounds the problem by letting operations get out of control. The company continues to produce to overly optimistic sales projections, physical inventories become bloated, and labor, sales and administrative staffing continue at levels required to meet the excessive production schedule.

"Usually, there's enough fat on the bone that management doesn't focus on the problem until cash flow starts to dry up," Getzler said. "Then the first reaction is to try to raise more cash. Cash is like an aspirin: it will keep the fever down as long as it lasts but the disease is still there ready to resurface."

Jim Mayer, president and chief executive of Dallas-based DiversiCorp Inc., another crisis management/turnaround consulting firm, sees a critical difference between small and large companies on the verge of trouble. "Many small firms do not have the resources or economic clout to convince suppliers and bankers to ride out the storm with them. There is a tendency to get it over with rather than participate in a workout with a small or insignificant customer or bank client."

According to Mayer, large companies must guard against vital information getting lost in levels of management and political infighting. Other warning shots across the bow include product and inventory obsolescence, delay or cancellation of new product introductions, dramatic changes in outstanding accounts receivable and accounts payable and eroding profit margins.

### Salvaging A Relationship

While many of A.E. Getzler & Co.'s clients are brought to the firm's attention by bankers and other lenders concerned about the safety of their investments, suppliers and customers of the troubled company often provide the catalyst for an ailing company to seek DiversiCorp's consulting expertise.

"Suppliers and customers have day-to-day contact and often see trouble on the horizon before company management focuses in on the problems," explained Mayer. Outside companies get in the act to help salvage a good business relationship with the valued customer or supplier.

Before 1986, turnaround consultants were on their own. There was little empirical knowledge about turnarounds and workout situations except that gained personally or learned from other consultants. Through the efforts of P. Scott Scherrer, the Turnaround Management Association, Chapel Hill, N.C., came into being.

In conjunction with the Frank Hawkins Kenan Institute of Private Enterprise at the University of North Carolina, Scherrer, now executive director of the association, initiated an investigation of business failures and the turnaround

process. The study involved interviewing more than 80 nationally known turnaround managers, analyzing more than 300 case studies and holding several conferences and group discussions.

Scherrer points out that there are several phases of corporate deterioration that need to be understood. The early stages of decline show some erosion of cash, declining sales and several quarters of losses. The normal tendency is to blame a temporary dip in the economy. The midphase sees a rapid building of inventory with subsequent large drains on the cash position. Finally, the late stage sees the company in a negative cash position and getting into trouble with bankers and suppliers over missed payments.

Both internal and external factors can spell trouble for the company. Too often, external forces are deemed hostile by management and beyond its influence. The internal environment, such as finance, production and marketing/distribution, is most easily controlled by management but paradoxically the most often uncontrolled.

### Warning Signs Ignored

Managers often do not realize they can plan for external changes and protect their businesses. Early external warning signals that often are ignored by management include economic growth activity, credit and money market trends, business population statistics, price level changes, changing technology and legal and political changes.

Although every turnaround is unique, Getzler, Mayer and Scherrer say that tough questions must be asked and answered. Internal reports must be examined carefully and individual sales and production managers must be made accountable for the accuracy of the information.

Production inefficiencies and inventory imbalances must be promptly identified to help reserve cash flow, the lifeblood of the organization.



Getzler