Turnaround Management Association®

Romania

TMA GUIDELINES FOR THE FIRST 100 DAYS

Principles in Early Turnaround

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TURNAROUND MANAGEMENT ASSOCIATION ROMANIA

Contents

Introduction

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The actions taken in the first 100 days (or even less in some cases) are critical in a stress situation, often making the difference between a success story and a failed one. They usually revolve around situation analysis, short- and medium-term planning and **acknowledging turnaround as a company goal**. Once the company is stabilized, management can then focus on the long-term strategy for turning around the Company.

When discussing amongst us with regards to the actions taken at the beginning of a turnaround or restructuring case, we realized that there are a few consistent themes that occur in each case. They revolve around:

- **Stakeholders' trust (investors, banks, suppliers, clients, staff) – *all of them are needed for a successful restructuring***
- People and the team in charge with turnaround the company – *someone who takes the project on board and drives the entire organization around this goal*
- Operational matters – *quick review of the operations of the company to identify pain points and propose solutions for those, incl. KPIs*
- Legal matters – *understand the level of protection needed by the Company and how can that be achieved, impact of existing and potential new litigations*
- Financial matters – *focused mostly on liquidity rather than budgeting*

This guide gathers in one place the experience of our TMA members, all of them experienced professionals in turnaround and restructuring.

By no means is this document meant to be an exhaustive one. It merely aims to provide some guidelines to managers out there in how to approach the beginning of a turnaround or restructuring case. We are sure each reader will have its own experiences and in case you would like to add to our guide, we encourage you to share your story at office@tma-ro.org.

We hope this Guideline will provide - both for restructuring specialists (whether they are employees of banks or consulting companies) and for the management of companies and entrepreneurs - a point of reference regarding the necessity, working methodology and analysis requested by an Independent Business Review.

Stakeholders' trust

"It takes a village". As the saying goes with raising a child, the same applies to a successful turnaround / restructuring. One way or another, at a smaller or larger scale, it needs the contribution of all stakeholders.

In case of failure, everybody loses. As such, the initial mindset is of "how can we help?". The key would be to preserve such mind set throughout the restructuring process and this is generally achieved via two main pillars:

No surprises

Constant communication is key.

Your stakeholders should be informed about changes in the company and their potential consequences. Short term, probably those consequences are negative, therefore it is important to show them the long term gains for staying next to you. A few examples are:

- Inform employees around the plans and allow them to share concerns, as well as invite them to participate in the process;
- Inform lenders and main supplier(s) / client(s) around management changes;
- Inform the lenders and suppliers in advance in case you estimate delays in payments and propose a plan for late repayment of those;
- Inform the clients in case of delays in deliveries;
- Inform shareholders in case you estimate results lower than estimated;
- Offer management meeting with main stakeholders, explaining the situation and how you plan to address it, as well as constant "reporting on results" meetings;
- Provide reliable and honest information etc.

In case of listed companies, the market will react significantly quicker than for a private company. A crisis manager is often hired, to ensure consistent communication to the market, via several channels (stock exchange reports, written press, social media), using appropriate language for each channel.

Delivery on results

Underpromise and overdeliver is better than overpromise and underdeliver.

Make a plan that you can deliver upon, including relevant measures to be taken. A good split of these measures (and therefore results) is based on how much you control the decision-making process:

- Full control: lay off decision; org chart changes;
- Partial control: sale of an asset / line of business; change of contractual terms;
- No control: taxation and legislation changes (e.g. increase in minimum pay, various taxes)

The measures in the company's "full control" should be fully achieved, whilst from the "partial control" ones, the company needs to do their share of the action. For the ones "no control", if some of them are known (like a new tax to be introduced), the estimated impact should be included in the overall plan.

In case the plan is not met, clear reasons should be given for this, as well as actions to address those.

People

At the end of the day, a successful turnaround is delivered by people, therefore it is key to pick the right ones to embark on such a journey.

Having the right project leader is critical. Operational and industry background, the ability to quickly grasp the essentials, without the benefit of comprehensive analysis, as well as charisma to inspire change are prerequisites in the process. She / he and can come from within the organization and from outside, as interim management / Chief Restructuring Officer (henceforth "CRO") for the process.

Top management support is key. The existing or new Chief Executive Officer (henceforth "CEO") needs to communicate constantly (*once again, communication is key*) to the organization that the turnaround process is key to the firm and that support is to be given to the project leader to achieve this. Our experience shows that if the top management (existing or new) does not constantly market the project and its importance, even if a few middle managers and staff are willing to adjust the way they work, the process will fail, as the goal is not perceived as a common one for the full organization.

Change is difficult. We are, after all, creatures of habits. An eye needs to be kept on those key individuals who refuse to make things differently, who "know better", i.e. who are not willing to collaborate. In some instances, they will need to be downgraded / made redundant, so that the entire process is not jeopardized. On the other side, the talent ones need to be retained, as they will act as drivers of the process in their respective areas (i.e. a good plant manager, a good logistic manager etc).

Once the Project leader and the team are assembled, the actual turnaround process is ready to start.

Financial Dimension

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Before going into what needs to be done during the first 100 days, it is important to understand that a turnaround / restructuring process costs money. It should be seen as a short-term investment for a long-term gain. That is why, the sooner such processes start, the better. If liquidity is tight (which usually happens is no advance measures are taken), attracting talent (internal and external) to work on the restructuring is very challenging and restructuring options are generally limited to in court options.

Furthermore, the outcome of the assessment and actions derived from operational and legal matters (e.g. change of contractual terms with a supplier / client, impact of potential litigations / redundancies etc) need to be considered in the financial management of the turnaround project.

Short term liquidity (13 weeks cash flow)

It is imperative that the short term liquidity position of the Company is constantly understood and immediately addressed.

The short-term cash flow is usually built via a direct method, as it is expected that management has visibility over cash inflows and outflows within a 13 weeks horizon. The first version of the cash flow ("As Is" version) needs to be carefully reviewed, to understand if various adjustments are needed (to derive to the "Adjusted cash flow" version). For example:

- In case one week is tight in cash (i.e. one-off nature), some payments to suppliers might need to be postponed
- In case of a more recurring nature of tight cash flows, short term actions will need to be taken to ensure sufficient cash is available for the turnaround project, such as:
    - Sell non-core assets, incl. idle equipment (might need to sacrifice profits for cash). In practice, the non-core asset / idle equipment is generally pledged in favour of a lender; the company and the lender(s) generally negotiate a deal, by which the proceeds from the sale go partially against the debt service (note: additional collateral might be requested by the lender, in case of partial payment), whilst the rest can be used by the company for working capital purpose.
    - Postpone payments to suppliers or simply slow down payments. With limited impact to the overall business, better payment terms can be negotiated with suppliers, one by one.

      Counterintuitively, the company can prepare for a rainy day by paying vendors a few days early. This buys goodwill and the vendors will most likely graciously extend payment terms when times are bad for the company.[1]

      Another approach would be to negotiate an expanding payment term agreement. The supplier gets paid on delivery for the first order, 30 days for the second order, 60 days for the third one, 90 days starting from the fourth one. [2] Or this can be reversed, depending on the cash constraints of the company and whether the situation can be solved within the first 100 days or so.

[1] (Sands 2020, 80)
[2] (Sands 2020, 88)

- Ask for early / advance payment from customers (this might carry and extra cost). If not in place yet, enter in factoring agreements with lenders, by which the company gets a certain percentage from the value of an invoice in advance (of course, bearing various commissions and interest).
- Invoice part of the work in progress
- Improve inventory management: (i) Disposing of old / obsolete inventories. The company could sell at a steep discount redundant/unusable inventory items even if it hurts the income statement and the balance sheet. This might be more challenging in case the inventory is pledged in favour of a bank. If this is the case, inventory might also be repurposed;
- Reduce CAPEX as much as possible
- Reach standstills with the lenders – please refer to the Legal dimension chapter

All these measures are to be communicated to the relevant team members for implementation. Furthermore, the outcome of any operational and legal assessment will need to be included in the "Adjusted cash flow", to ensure all items are fully captured[3].

The Adjusted cash flow will be the version constantly updated and monitored. Usually, a short term cash flow should be updated weekly. However, due to ongoing business activities and system limitations, this is not always feasible, therefore, in practice, such cash flow is drafted every two weeks.

It is normal that the first versions of the 13w cash flow be less accurate, but, after several iterations (usually cca.5-6) the process becomes automated, accuracy increases and less and less time is spent on it.

Key items to consider when developing a short-term cash flow:

- Make sure only available cash is considered (i.e. exclude any restricted and trapped cash)
- Use probabilities for cash inflows (i.e. if there are inflows you are unsure of be prudent in considering those as cash inflows) *(Note: teams are usually very optimistic on inflows, therefore inflows need to be scrutinized)*
- Assume a payment schedule to suppliers that you can stick to (as mentioned above, stakeholders trust is critical, therefore if you commit to a payment schedule to one supplier, you should keep it)
- Add any cash outflows related to restructuring payments / workstreams
- Make sure there is always a minimum cash balance available for the use of the company

Once a new version is drafted, a comparison with the previous version is required to identify differences, that can usually be divided into:

- Temporary differences – that will unwind over the forecast period and
- Permanent differences – for which relevant causes need to be identified and new actions need to be proposed.

The short-term cash flow forecast should be developed as long as the company faces cash pressures and should be a primary tool in any turnaround and restructuring project.

[3] In case the Adjusted Cash flow results in constantly negative cash (i.e. the measures to be taken are not sufficient to generate positive cash flows), it is recommended for the company to consider a reorganization in insolvency

Budgeting

A first draft of a budget needs to be developed in the first 100 days. Similar to the cash flow, it should start from the As Is situation and add the impact of any operational initiatives aimed at increasing EBITDA as well as any restructuring costs.

The budget should be developed monthly for the first year, followed by annual estimates until year 5. Please note, such long-term estimates should consider the long-term strategy of the Company, therefore it might not be possible to develop them in the first 100 year. In any case, a monthly budget for the first year of the turnaround process is mandatory.

If several business lines are in place, a budget for each needs to be developed, that is then consolidated into one budget for the firm. In the first 100 days, having a P&L drafted should be sufficient, but this has to be completed with a cash flow and balance sheet at the earliest convenience.

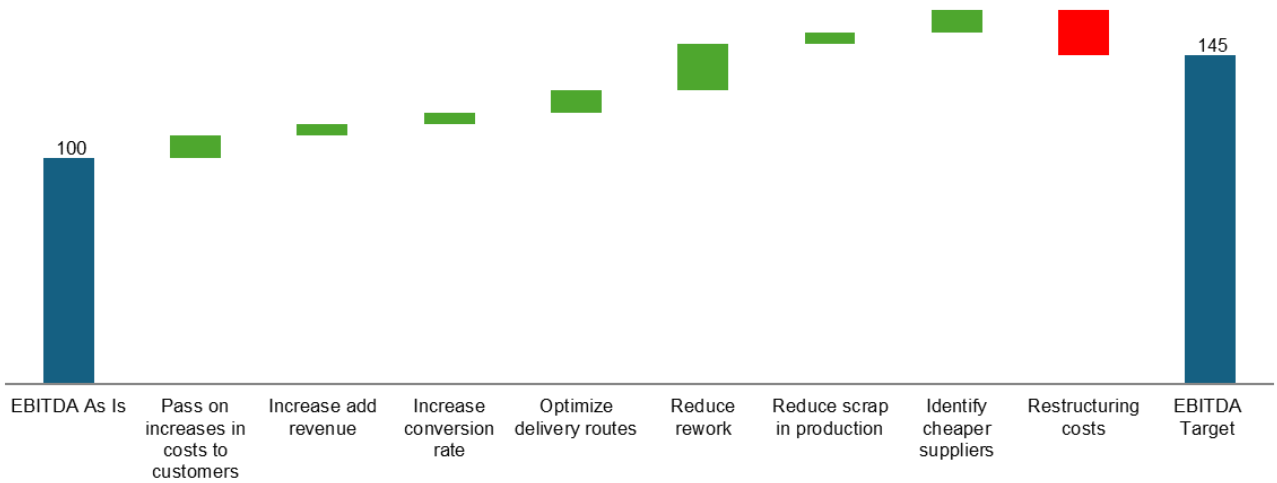
Medium term (post the 100 days period) a clean-up and remodeling of the balance sheet might be required:

- Illustrate the "real" working capital, i.e. excluding old receivables / inventories
- Restructure debt and overall liabilities, so that i) short term assets match short term liabilities and long-term assets match long term liabilities and ii) the company has a sustainable level of debt.

Any initiatives developed in the operational workstreams needs to be measurable and quantifiable in terms of EBITDA contribution (as well as have a timeline for implementation with clear milestones and KPIs), as to enable the Project manager to track results and intervene when relevant. We have listed below an illustrative EBITDA bridge from an As Is version, to a Target version.

Bridge EBITDA As Is to EBITDA Target based on initiatives examples

Note: initiatives below are taken from companies in various industries, and are not by any means exclusive



Operative Dimension

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Generally, organizations are stable systems. At some point they become destabilized due to lack of direction and lack of control which constitute management and leadership failures.[4]

Employees who were used to operate within a stable system will have established behavioral patterns tailored to the predictable environment. Before the turnaround process starts, external, internal disturbances or a combination thereof will effect changes within the corporate inner environment. This leads to people increasing their inner and outer volatility, centrifugal forces will begin to be felt, their learned behavioral patterns no longer adequate.

The brain is essentially a prediction machine. Due to this core feature, focus will shift from productivity to scenarios construction which additionally saps general energy. Rumors and gossip, the lifeblood of organizations, will become toxic, further increasing the centrifugal tendencies. Furthermore, mindlock can occur, leading to people having less and less control over their own bodies. This can be compared to bodily reactions during life threatening events.[5]

It is clear that whoever takes on the mandate of fixing the problems will enter a world of high anxiety and distrust. Armed with the tools laid out in the Financial Dimension, he will have to bring to bear razor-sharp focus and iron determination. The principles to follow must be applied constantly in order for results to materialize. Only a disciplined mind can zoom in on some problems and at the same time zoom out to understand the larger picture. Since time, energy and allies are scarce, only a careful ranking and balancing of the presented issues will lead to mastering the challenges in a difficult and unfriendly environment. The turnaround practitioner must possess a wide-ranging skillset and be able to grasp widely varying issues. Most of all he/she must be able to integrate them in a cohesive whole and communicate adroitly.

When a turnaround starts is up to the entrepreneur or other key stakeholders. This is not to be confused with the time of when a turnaround should start. Experience show that it usually starts later than ideal. There is an ideal distinction made between turnaround and restructuring. Turnaround should be out-of-courts and before creditors are aware of problems and it therefore should represent a proactive approach, led by the company. Restructuring should ideally be out-of-courts when initiated and finalized. There are cases when the case begins out-of-courts and ends in-courts. Relying on one or more events-of-default as the trigger, the restructuring process is more of a reactive approach, with the banks having a considerable influence in the process. [6]

When a turnaround ends is easier to ascertain. It depends on the mandate, or the understanding of the professionals employed. Below indicative moments are shown of when a turnaround can be declared to be finalized:

(i) After the company is stabilized
(ii) After the business is refocused/ or fixed

[4] (Slatter, Lovett and Barlow 2006, 11)
[5] (Sands 2020, 57)
[6] (Lascu 2024, 566). There is significant confusion regarding the terminology. The author offers some clarity as to the fine distinction

(iii) After the company is rejuvenated and a new organizational culture is embedded.[7]

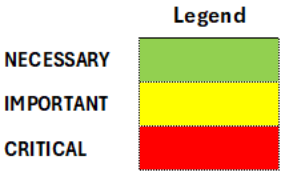
In the case of the First 100 Days that is the subject of this paper, the turnaround would ideally start when the entrepreneur sees incoming stormy clouds, before this can be seen in the financial results by a financial lender, and it would end as a stage when the business is at least stabilized and ideally also refocused. To fix the underlying problems of business would require at least another 100 days.

In essence, all types of turnarounds from mild downturn to profound crisis are based on getting everybody doing what they are supposed to do: customers buying, workers working and the bank lending. Only if this is achieved can the turnaround process work. So, "get everyone through the turmoil, establish complete control and buy time to address the core issues".[8]

Turnaround Key Ingredients

The following are key ingredients that are required in order for a turnaround to be successful and these have to be tackled either from a management or leadership perspective, or a combination thereof.

"Managers rely on systems, leaders rely on people. Managers work at getting things right, leaders work on the right things."[9]



	Management	Leadership
New Leadership		
Crisis Stabilisation		
Stakeholder Management		
Strategic Focus		
Critical Process Improvements		
Organizational Change		
Financial Restructuring		

NB: Departing from the authors[10], for the first 100 days, strategic focus is necessary but not important, financial restructuring is important but not critical. This criticality is based on our judgment on what seems to be most common to encountered in turnaround cases. Depending on the severity of the situation, financial restructuring can become critical.

Leaders should not get bogged down in daily operations but they should rather manage organizational context. As such, they must create the conditions that are conducive to a good functioning of the company.[11]

[7] (Slatter, Lovett and Barlow 2006, xi)
[8] (Sands 2020, 73)
[9] Richard Kovacevich, CEO & Chairman of Wells Fargo Bank in (Slatter, Lovett and Barlow 2006, 9)
[10] Author's adaptation to the first 100 days context, ranked according to criticality from (Slatter, Lovett and Barlow 2006, 13ff)
[11] According to Harward Business Review, 2004, in (Slatter, Lovett and Barlow 2006, 9)

New Leadership

The entrepreneur's/CEO's reaction will have an outsized impact on the business and whether it becomes a failure or a success. If necessary, the entrepreneur/CEO himself must be jolted into action.

Management style has to change immediately. Inclusive management is of course the desired norm in a company, however in a crisis situation, the overly bureaucratic/cooperative decision-making mechanism will not yield the flexibility and speed required to address the multitude of challenges. Brain freeze will also not be lifted by inclusive management. Accordingly, the style of management must become more firm to the point of being authoritarian. It must trade comfort for efficiency in order to generate and maintain strong and unyielding resistance to centrifugal forces. The leader has to step to the frontlines and ideally the responsibility should lie with him.[12] [13] Turnaround and crisis management are not about armchair quarterbacking. Turnaround is about being in the trenches, close and engaged with the people. It is about leading by example and assuming responsibility.

Linked to turning around the mindset of the entrepreneur/CEO is the need to rapidly build a new management team or develop a core team in charge with driving the process. If there are no resources for outside hiring of a critical mass of managers, then a reenergizing/ refocusing of the team in place must be achieved in order to be able to delegate part of the process of turning around the company. This is tricky and involves a lot of risk since the managers in place even though they know their industry, are usually woefully underequipped in terms of analytical and decision-making skills. They are also biased and view the company's history subjectively and therefore are most of the time mentally unable to take the hard decisions necessary to perform critical changes.[14]

The turnaround practitioner can be in an advisory role, alongside the CEO or ideally or for more complex cases, assume line management and Board level responsibilities as CRO.

The CRO traditionally focuses on crisis stabilisation, stakeholder management and financial restructuring. The CRO can act as special advisor to the chairman, the CEO or the Board with the mission of turning around the company. This type of C-level executive originated in the US. There is an increasing demand for CRO services due to increasing complexity of capital structures even in the case of mid-sized companies and as a result the financial restructuring process. The chairman and CEO usually don't have the expertise or the time to lead complex financial restructuring in parallel with an operational restructuring.[15] In developed countries both CEO and CRO can be afforded at the same time, in emerging economies it is usually one or the other.

The CRO also has the option to build his turnaround implementation team around outside sourced Interim Managers, experts for very specific tasks who can act as a fire-fighting squad. These have full buy-in to the process and can be effectively and surgically delegated. Following from this, a good principle is that the CRO must know his own limitations, which is an essential prerequisite to good leadership.

[12] (Sands 2020, 56)
[13] (Slatter, Lovett and Barlow 2006, 104)
[14] (Slatter, Lovett and Barlow 2006, 6)
[15] (Slatter, Lovett and Barlow 2006, 2f & 118)

Stakeholder Management - Internal

People at the ground floor know that things are turning sour. If the intent is corporate renewal, then the last thing the leadership wants to do is not being frank about the situation. The best thing that can be done is to improve communication inside the company to with clear messaging. By now, mistrust has set in and people must feel that the organization is communicating again.[16] After officially recognizing the difficult environment, the key point is to refocus their attention on what is actually important, away from redundant or unproductive activities.

Since worrying is also an unproductive activity it is also very important to give reassurances. A turnaround professional has been involved in several special situations and knows the process. Due to this, the path out of the mess is known by him and this must be communicated clearly to the people.[17]

Every employee is different, but only some can be refocused and rehabilitated. Some have to be handled gently while other need to be shocked, hopefully into action. There are some that might have high potential but have most likely been sidelined and must therefore be coopted and encouraged.[18] Employees are generally afraid of turnarounds. What most don't understand is that such a process brings great opportunities to people that are high achievers or who have a mission-oriented mindset. In the words of Jeff Sands, a Certified Turnaround Professional (henceforth "CTP"): "Turnarounds are an opportunity for heroes. I give plenty of speeches about how some clever employee is going to take advantage of this situation and rapidly advance their career by helping, while others sit back with an "I'll just see what happens" attitude. A few employees will see the opportunity and take matters into their own hands. I tell everyone they are free to make changes. We are determined to work smarter and if you want to make changes, come see me and I'll start approving your changes. Want to really shake things up, I'll give you all the rope you need."[19] The role of a turnaround practitioner is to enact change management. He must essentially be the fulcrum and catalyst of all positive changes within the organization. He must become the go-to agent for everyone in the company.

It is also paramount to build a trusting environment, allowing for the occasional merriment since employees will be asked to increase their workload substantially while at the same time becoming accountable for their work [20] (as a result of the below balanced scorecard-type performance management). This also helps with the retainment of some of the most capable and dedicated employees.[21] What needs to be borne in mind is that capable employees are cheaper to retain than to hire, so special care must be taken here. This general rule is especially true in a financially and reputationally challenged company.

Ideally, a turnaround should start from the Finance Department with CFO and Controlling fully on board. At the same time, it must be communicated to all departments that the turnaround manager/consultant/CRO will eventually get in touch with their respective departments and that in the meantime they should perform their duties to the best of their abilities.[22]

[16] (Slatter, Lovett and Barlow 2006, 33)
[17] (Sands 2020, 63)
[18] Ibid.
[19] (Sands 2020, 68)
[20] (Sands 2020, 63)
[21] (Slatter, Lovett and Barlow 2006, 34)
[22] (Sands 2020, 63)

Organizational Change

Similarly to the way in which turnaround practitioners are able to rank the severity of the technical issues, they must also be able to honestly rank employees according to their abilities, involvement and character. A stable environment affords all types of employees, whereas an unstable environment requires the empowerment of only certain types of people in order for the company to be able to heal.

a) Seek Out Character

If any of the core positive traits is lacking, there will be trouble, these being ability, involvement and character. However, there is a grading to them. Imagine, for example, what a person with high energy and ability but without character can do to an organization and to the corporate stabilization process which is essential to the going concern of said organization.

Without discarding the need for civility and team spirit, a turnaround practitioner must reverse the proliferation of the yes-man mentality and people pleasers inside the organization. People pleasers are antithetical to the success of an organization in a distressed situation. They are either sitting back, deflecting or working solely for their own benefit which generally means against the actual interest of the organization. In front of their teammates and superiors they will lie, hyperbolize, cheat and obscure the salient issues so that the corporate stabilization and refocusing processes will work in their favor. The danger is that that these processes could be become derailed.

Consequently, people without character must either be given limited roles within the process or isolated from it. People with character are natural allies to the turnaround practitioner.

Another principle to consider which can be healthy for the organization is to feed heads to the stakeholders, to make it clear that change has begun. Mistakes were made and people want justice. Lenders also want to see blood since they might be asked to put their money at risk. This measure signals to the customers, vendors and lenders that the process is sincere and that the company is on the path of becoming a better partner. Selection criteria can be: (i) complaints from many people, (ii) people who resolutely stick solely to their job descriptions and who openly advocate for it, (iii) people who misappropriate company resources e.g. people literally sleeping at work, people who charge fictitious overtime, people who don't perform their duties adequately but have a side hustle, people who committed fraud. The fraudsters and perhaps also the side-hustlers (unless they understand that the game has changed and change their behavior) must be fired immediately. In the case of C-level or management firings, these must be communicated to the bank. This serves several purposes: it sends a message, it dissociates the rest of management from the problems and most importantly, it protects the company. [23]

b) Reward Involvement & Ability

As we are talking about the inflection point from normal to crisis, a stable environment will suspend to a considerable degree the Darwinian forces of selection. This leads to wider access and greater distribution of resources, "waste" in short.

The important thing to remember is that even though environment is now unstable, through the efforts of the turnaround practitioner/CRO/Interim Manager it has become fairer and employees are starting to be recognized for their abilities and capacity to deliver. That is a key distinction, and it will lift a lot of stress from the shoulders of the employees with the results of emboldening workers to start working.

[23] (Sands 2020, 71f)

Establishing Control – Measuring Performance

Many companies evaluate employees based on qualitative criteria, subjective criteria which leads to lack of standardization, which leads to lack of comparability, which leads to the company having performance management in name only. Establishing effective performance management is key in measuring performance and driving performance. A 100 Days process does not have time for a full diagnostic and implementation, however something quick and dirty must be implemented.

The Balanced Scorecard (henceforth "BSC") as a strategy performance management tool designed to keep track of staff activity execution is meant to address a corporate culture which does not value clear understanding of who is doing what, leading to waste in people resources, overlapping competences, redundant work such as overreporting, or reporting of irrelevant matters.

Objective of the BSC:

1. Communicate to everyone what the organization intends to do
2. Alignment with the strategy of the day-to-day activities between management and employees
3. Set priorities for projects, products and services
4. Measuring and monitoring progress to meet strategic targets
5. Using financial indicators coupled with strategic indicators
6. Vision + Skills + Incentives + Resources + Action Plan = Change

The turnaround practitioner must focus depending on what is lacking. The quick development of the above must lead to buy-in to the vision by employees as well as managers.

Stakeholder Management - External

The communication with financial lenders must be frequent and open. It is crucial to build trust so that support is achieved that will create a window of opportunity to solve the issues. It might also be the case that some banks refer the crisis manager to the turnaround position

Research found that good leadership is important also before the turnaround is initiated. Ideally, good leadership should start months in advance of the turnaround process, to guarantee stakeholder commitment for when the corporate renewal process starts.[24]

Banks can have a key leadership role in initializing the turnaround process. The appointment of a CRO is increasingly becoming a precondition of support by financial lenders.[25] For cases with complex capital structures, workout officers will only be able to sell the rationale for emergency financing, debt moratoriums, haircuts to the credit committee if there is a C-level in place, who is fully aligned with the bank's and the company's interests and who knows just how streamlined the turnaround process must be. In an interim role and as an outsider looking in, he will perform a dispassionate assessment of the situation and since there is no history with the company, he will be able to carry out the reforms necessary for the company to stabilize and then to rebound.

[24] (Slatter, Lovett and Barlow 2006, xi)
[25] (Slatter, Lovett and Barlow 2006, 4)

Critical Clients and Suppliers – Understanding Negotiating Power

Below items are discussed in terms of achievability in light of the respective negotiation power of the ailing company vis-à-vis its critical counterparts.

- Increasing prices: There are a multitude of reasons why prices should not be raised, however when the stakes are high, there is a good rationale to do just that. Of course, it clearly depends on whether we are talking about B2C or B2B and the type of company, but herein shown advice is in essence principles-based.

  Prices can be raised one by one in a controlled process. There is also business that should be retained and business that should be chased away. Sometimes there is the need to even sacrifice future business to preserve the present. Depending on what the company is offering, resourcing by the clients of the turnaround target company can take from 1 month to 1 year. They key point here is to generate the short-term cash which will bridge the company to allow it later to fund a retention strategy of important clients.[26]

- Collecting faster: This can start with the best customer(s) since they are more likely to help out. Good customers can also be offered cash discounts to entice them. One idea which is used extensively is factoring, however the ailing company should not get overly exposed to factoring since in time, the associated cost will compound. Great care must be taken about the type of customers involved when showing weakness. Big retailers might dump the company immediately upon it showing weakness. The mentioned financial instruments of factoring will help in this regard as well, speeding up the collection process while helping while helping not to weaken the company's negotiating position. Customers with long lifecycles like auto, aerospace or pharmaceuticals will likely be compelled to help out, since the ailing company is a cog in the value-chain process, which can derail the entire process. The company cannot be easily substituted for an alternative, due to quality control issues, proper available stock etc.

  If there is sufficient leverage, immediate payment can be demanded. It all depends on where in the value chain process the distressed company is.[27]

- Partner up with the clients or suppliers: The turnaround practitioner of the distressed company can make the case to a client/group thereof or a supplier/group thereof that they should invest in the company. This is especially true if a counterparty is critical, with significant leverage over the company. In this case a debt-for-equity swap[28] can be arranged. This is a risky moment for a helping counterparty since there is an information asymmetry involved. Therefore, we reiterate the need for forthright presentation of facts. Otherwise, counterparties could start preferring insolvency proceedings over more out-of-courts measures.[29] Alternatively, a debt-for-credit swap can be arranged, meaning short-term supplier credit in exchange for a long-term loan. Also, being a new face, the turnaround practitioner can also negotiate with core suppliers to freeze past-due balances while increasing the credit terms plus also maybe open a credit limit.[30]

- Centralizing Procurement: so that either the CEO or the CFO approves procurement

- Debt default: if the company reaches a severe liquidity crisis, then defaulting on the loan might be the only course of action. We recommend being fully aware of the implications. Even if the loan(s) are not effectively collateralized, should the company not repay them, they or the owner will have

[26] (Sands 2020, 78)
[27] (Sands 2020, 79)
[28] (Sands 2020, 190)
[29] (Gaughan 2018, 467)
[30] (Sands 2020, 85)

difficulty in the future of being credited by the banking system. We recommend that a company in such a situation be aware of what this entails: increased scrutiny by the bank, increased time allocated to communication and information requests and prolonged negotiations. Under certain scenarios it can also be that credit lines might be accelerated and the collateral enforced by the bank.

The Income Statement Turnaround

Turning a cash-losing business into a cash-generating business by first stabilizing it by focusing on the cash flow as discussed in the Financial Section, to then be able to turn to the income statement, where the actual turnaround takes place.

Ownership remains unchanged
• As a principle, the CEO or Turnaround Practitioner needs to drive revenues to exceed cost, and it must do it consistently. Increase sales volume as quickly as possible. Make the entrepreneurs focus on sales and operations
• Increase gross profit margins through price increases and cost cutting during the first 100 days. After this period, more fundamental changes must be made to underlying production processes or services • Furthermore, the CEO must also become the Chief Profit Officer, squeezing pennies out of the business, to provide greater stability: professional purchasing, better scheduling to reduce direct labor, indirect labor.[31]
• Shrink the business to profitability as soon as possible (or divest). Sustainable profits and core strengths are the target. A large turnover sounds impressive. Wanting to cut it in half will raise the hairs on entrepreneurs and owners, however this must be done to reach a sustainable size which will allow back growth.[32] Retrenchment is a skill and it requires coordination of all activity dimensions of the company plus some of the short-term cash generated as a result of measures in the Financial part of the process
• Outsource as many secondary functions as possible
• The turnaround practitioner must coach the entrepreneur to not get ballistic, which can poison stakeholder relationships, even destroy key assets of the company as a result[33]

The Balance Sheet Turnaround

This type of turnaround involves all types of business, from healthy to distressed (income statement-wise). What they all have in common is a crushing debt service level, and as a result they all experience cash constraints.[34]

[31] (Sands 2020, 135f)
[32] (Sands 2020, 141)
[33] (Sands 2020, 147)
[34] (Sands 2020, 25)

Business model

There are five important principles to keep in mind when addressing a turnaround and its chances for success:

1. If money is being lost, then the business model is broken.[35] It becomes clearer and clearer that the current business model has reached its useful life
2. Only a formerly profitable company has good chances to be turned around[36]
3. During the first 100 days, a turnaround process will not be able to address the underlying causes of distress. Trying to fix everything wrong with the company is a bad idea
4. "The bottom line is that a turnaround will be some formula of raising prices, cutting costs, streamlining operations, and fixing bad habits"[37]
5. Turnarounds are mostly about leadership, not management. The earlier in a turnaround, the more leadership is required. This balances later on, however, leadership will still be more important than management

Review Product Offer & Turnaround

Several examples are offered by Jeff Sands, CTP in his book[38]. Two examples are also offered by the author:

No.	Issue	Solution
1	Production company with a lean backlog and meagre margins	Invest in marketing, increase prices while investing in the sales department in order to reach a wider customer base to offset the loss of customers due to said price increases
2	Transportation company driving expansion while ignoring maintenance CAPEX coupled with timid pricing for the products so drivers leaving to drive better machines	Increase prices and focus on core products (forget about unproductive lanes)
3	Retailers/distributors with stale inventory and lack of cash	Quick inventory disposal process and footprint shrinking leading to the ability to buy fresh goods to resell
4	Company with smart even brilliant entrepreneur who is also self-destructive: it has good products, exceptional engineering, good service but a broken supply chain and no cash since a sizable part was spent on vanity project	If ego gets in the way, the best scenario is foreclosure and with the new owner the former entrepreneur can focus on his strengths without the headaches of being an entrepreneur

[35] (Sands 2020, 132)
[36] (Sands 2020, 132f)
[37] (Sands 2020, 135)
[38] (Sands 2020, 133ff)

5	Manufacturing business with a plethora of demanding and high-maintenance distributors which costs money and focus	Ranked distributors according to contribution margin and aggravation and then the bottom-ranked 25% ceased to be a counterparty to the company
6	Production company with a product catering to a single customer type	Make that product interesting for other customer types and use adroit marketing to do so. In this case a high volume-low margin product, after a bit of tweaking, started being marketed also as a high volume-average margin product
7	Integrated O&G producer which chose to diversify to offshore construction and invested aggressively in large assets	Sale and lease back of some of the assets

Hopefully the above has worked. In case it didn't, the company is about to enter even more difficult territory.

Ownership changes
"Most entrepreneurs overestimate their ability to shift momentum and underestimate the damage done to their business over the years"[39]
• The turnaround practitioner must focus on drafting confidential information memorandums (henceforth "CIM") for strategic buyers which must focus on core company strengths while at the same time not letting buyers get distracted by all the issues[40]
• The CIM must present the highest going concern value in order to reach a binding letter of intent (henceforth "LOI") which can help with bridge financing[41]
• The buyer's top executives should be walked throughout the plant floor to show them every little opportunity available to them. **The entire P&L and B/S is walked on foot while guiding them to an optimistic understanding of the business**.[42]
• Everything which has or potentially could have value must be sold: revenue, backlog, project pipeline, unique capacities, redundancy savings, future potential, know-how, intellectual property, position on the market, even personnel. Everything is up for sale.[43]
• Secure employment contracts for the entrepreneurs. Achieve the full recovery for the bank[44]
• If the above fails, turn to financial buyers. The process becomes more difficult
• If the above fails, turn to special situations PE firms. The process becomes even more difficult
• Last question is whether the business would be taken over where it offered for free[45]

[39] (Sands 2020, 147)
[40] (Sands 2020, 148)
[41] Ibid.
[42] Ibid.
[43] Ibid.
[44] (Sands 2020, 154)
[45] (Sands 2020, 151)

Legal Dimension

Contributor: Valentin Voinescu, TMA Romania

The legal component of the turnaround process needs to work hand in hand with the operational and the financial, as critical components of a successful plan. Seamless communication between the three, as well as a solid educational foundation cross-specialization, are critical.

The legal strategy looks at three essential elements:

1. Evaluation and Diagnosis

Critical due diligence must be performed to properly identify and understand the following areas. First of all, any direct risk of enforcement or insolvency must be assessed, including key assets at risk. It is also important to identify any other major litigation, whether current or pending.

Attention should also be given to:

a) elements of fraud, illegal or unethical behaviour;
b) prima facie detailed simulation of the insolvency table and likely outcome of major distress - will the likely outcome be bankruptcy, is there a possibility for reorganisation, are there tools to consider for aligning majority creditors, etc.;
c) major disruptive events which may occur and compound losses if added stress occurs;
d) major "holes" in critical contracts, particularly major off-take, major suppliers etc.

2. Implementation of stakeholder containment, organization and harmonization tools

A good legal team will know how to address major "fires" and respond appropriately to immediate threats against equilibrium. These may include:

a) aggressive suppliers or clients filing court actions against the company;
b) disgruntled former managers or employees;
c) regulatory inspections on critical issues.

The team must also seek to successfully "hit the brakes" and avoid a disorderly enforcement outcome, by ensuring either by contractual means or by court procedures. At the same time, it must set up the requisite legal infrastructure to allow for an organized and properly managed turnaround, with the support of all key stakeholders.

3. Restructuring tools

There are many areas in which key legal advice is needed. These typically include:

a) **Employment** - redundancies, reorganizations, employment of new critical staff;
b) **Compliance** - major revamping of key critical areas previously missing, in key domains;
c) **Contracts re-negotiation** - a substantial amount of time is usually spent on readdressing key legal issues with key counterparties, on an ongoing basis until stabilization of the business;
d) **Agreements with creditors** - following a standstill, naturally the ideal position would be to be able to implement a restructuring plan, and this needs to be properly documented.

A strategic overview of the main legal tools available for implementing a turnaround

Effectively, there are four potential stages or options that can be pursued, depending on the specific circumstances of the company in difficulty. It is the responsibility of an experienced legal advisor-working in close coordination with the broader turnaround team, including financial and operational consultants, to assess which of these phases is most appropriate and feasible to support the restructuring objectives.

a) Out-of-Court Restructuring

This option is suitable when a high degree of consensus can be reached among stakeholders, and formal legal proceedings may not be absolutely necessary to force other creditors to adhere to the solution. It is typically most appropriate in the early stages of turnaround.

A key element in this context is the implementation of a standstill agreement, whereby creditors agree to refrain from enforcing claims for a limited period while restructuring terms are negotiated.

Standstill agreements

There is genuinely a lot of value in implementing contractual tools allowing creditors to act in a coordinated manner to preserve value. The key features of a successful standstill agreement are:

(i) implementing a standstill period during which the restructuring plan will be implemented;
(ii) establishing rules of transparency, information flow and organization of communication;
(iii) agreeing "cease fire" rules, including no enforcement, no litigation etc;
(iv) setting up viable and uncontroversial rules for termination

TMA Romania considers that a local adaptation of the London Approach (what can be called a "Bucharest Approach") is entirely feasible, particularly where the majority of creditors are banking institutions.

The main adaptations or amendments would be entirely to correlate the famous London Approach to the current Romanian legislations, in matters which are relevant for the solidity of the documentation and obligations assumed (including for example references to articles in the Romanian insolvency legislation that allow a suspension of the obligation to file for insolvency if the company is engaged in an out-of-court restructuring).

This approach is designed to manage corporate financial distress in an orderly and constructive manner, with the ultimate objective of preserving viable businesses wherever possible. It reflects a preference-shared by key stakeholders - for consensual workouts over the immediate appointment of receivers, even though receivers are bound to act in the interest of preserving business value.

The approach is premised on the idea that any restructuring proposal must offer creditors, especially banks, a recovery at least equivalent to what they would achieve through formal insolvency proceedings such as receivership. The approach encourages collaborative negotiations aimed at reaching pragmatic compromises-even if such outcomes fall short of any party's ideal position.

b) Preventive Arrangement (Preventive Concordat)

This mechanism is intended for companies facing financial difficulty, but not yet insolvent, as defined by Romanian law. Financial difficulty refers to a situation arising from any circumstance that temporarily affects business activity and creates a real and serious threat to the debtor's future ability to meet its

obligations as they fall due, unless appropriate measures are taken. Importantly, a debtor in difficulty remains capable of meeting its obligations as they mature.

The preventive arrangement, in particular, offers several benefits:

(i) it suspends enforcement actions during plan implementation;
(ii) until the restructuring plan is confirmed by the court, creditors may not refuse to perform, terminate, accelerate, or modify in a detrimental way any essential ongoing contracts due to non-payment of pre-suspension claims.

c) Insolvency Proceedings - Restructuring Agreement

Judicial reorganization is suitable for insolvent companies that maintain operational viability and creditor support. It allows business continuity under court supervision while a restructuring plan is designed and executed. The plan may span up to four years, during which the debtor can selectively maintain or terminate contracts based on their relevance to the recovery effort.

One of the key strengths of judicial reorganization is the structured nature of the plan itself. With the support of the court-appointed judicial administrator, the debtor must present a detailed economic assessment of the business, including the causes and severity of its financial distress. The plan outlines proposed restructuring measures-ranging from operational optimization to asset sales, debt restructuring, and even corporate transformations.

Additionally, the plan must include a comparative simulation showing the expected recoveries for affected creditors under the proposed strategy versus what they would obtain in the next best alternative scenario-often liquidation. This comparative transparency reinforces creditor confidence and supports approval of the plan.

d) Bankruptcy Proceedings

Though often linked to liquidation, bankruptcy can be strategically used to support a turnaround. In certain cases, it allows for the transfer of essential assets to a newly created entity, enabling the relaunch of operations while winding down the original, non-viable company. Within this context, pre-packed bankruptcy-where a restructuring plan is negotiated in advance and quickly approved post-filing-can be a valuable tool, ensuring speed, predictability, and reduced business disruption.

All these instruments share the common goal of enabling business recovery and long-term viability and should be viewed as complementary options within a flexible, case-specific restructuring strategy.

About the Authors

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Andreea is a Board Member of the Turnaround Management Association, Romania.

Andreea has more than 15 years of advisory experience. She is specialized in Business Reorganizations and Restructurings and has experience in Romania, as well as cross border in the UK, the Netherlands and Republic of Moldova, having spent 2.5 years in the restructuring practice of PwC UK.

She has advised both lenders and corporates in challenging situations (how to address new money/restructuring asks, extension of loan facilities, monitoring of distress companies etc.), going concern assessments, dealing with key suppliers who filed for insolvency etc. More specifically, she has led and delivered liquidity, business plan and portfolio reviews, assessed lender recoveries under various scenarios, options analyses and contingency plans.

She has a wider understanding of the Deals practice, being also a qualified insolvency practitioner and being involved in transactions, Valuations and NPL projects.

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He is a Partner in NNDKP's Banking and Finance practice, and, along with a diverse range of corporate finance mandates, is the principal coordinator of special situations and turnaround mandates for the firm.

Valentin has constantly advised across the years large companies, banks and investment funds on some of their most complex cases, in an ever-changing environment, starting with the 2008 financial crisis, and up to the current post-pandemic and conflictual environment.

Besides his legal training (passing with one of the highest grades the final Bar exam), he also holds an MBA from Vienna University.

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