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Denial revisited – with a twist

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All turn around/crisis management assignments require a willingness to deal with chaos, a thick skin to ignore the roadblocks thrown up by management, the ability to analyse unknown situations quickly and to devise and implement effective solutions, tenacity in execution and a talent for practical psychology.

The need to apply effective practical psychology first arises in connection with management's denial of the situation and the requirement that interim management effect a realisation of the unpleasant realities facing the business and the potential implications for management's future. How successful an engagement will be is in large part defined by how quickly management can be made to understand and buy into the need to confront reality and craft solutions that address that reality. Until this task is accomplished all of an interim manager's talent in analysing and correcting financial, operational and human relations problems are functionally irrelevant because none of the interim manager's message is heard and therefore few, if any improvements can be effected in the enterprise's parlous situation.

How an engagement is styled has a significant impact on how easily management's attention can be obtained and how quickly existing managers can be made to focus on the reality they face. Turnaround or crisis management professionals taking interim executive positions with clients face a significantly easier task in reversing denial than their colleagues who are engaged to act as advisers to the management team on whose watch the problems have occurred.

However, regardless of how the engagement is styled, achieving an appreciation of reality by management requires a delicate blending of fear and support by the crisis professional. Too heavy handed a dose of reality can cause management to shut down, leave or terminate/replace the crisis professional. Too subtle signals allow management to ignore the message until the enterprise implodes (precisely what the crisis manager was hired to avoid).

In addition to the nature of the crisis professional's role other factors come into play in determining how much of a professional's time must be devoted to the psychology of management denial and leading management to reality. Factors that routinely need to be evaluated in determining how much fear and how much support must be employed include how entrenched existing managers are, whether the enterprise is public or private, whether senior management owns a majority stake, whether senior management founded the enterprise or is related to the controlling equity group. A less well known factor affecting the ease with which management opinions can be altered to accept reality can be derived from the character of the industry in which the engagement is found.

Industries which are inherently cyclical and subject to great swings from prosperity to disaster and back to prosperity may well require a greater degree of psychological insight on the part of the professional than more stable industries. The degree to which management is subject to the vagaries of the market as opposed to being able to control

its own destiny also directly affects how tractable that management will be to change course to deal with the apparent disaster that led to the engagement of the turnaround professional.

Industries which fit this profile include shipping, independent oil and gas exploration and production, real estate and oil and gas service providers. These industries are subject to a degree of political and economic volatility. The volatility of these industries puts a high premium on self reliant personalities who survive by overcoming obstacles which most people would shrink from even contemplating. This attracts risk takers who bring such strongly optimistic psychological profiles with them when they first join the industry. Typically, the risk takers are the founders and senior executives of the independent and maverick players on the margin of these industries. As smaller more nimble participants they seek to take advantage of arbitrage opportunities which arise because of relatively temporary imbalances in the market. To maximise those advantages these players frequently resort to high degrees of leverage which maximise returns on the upside but can crush an enterprise when the market goes sour, even for a short time.

For example, many of the great shipping fortunes have been made by entrepreneurs who play in the spot market where their companies are at the mercy of daily changes in supply and demand for the ships they own and operate. These entrepreneurs could enter into long term charters with credit worthy users of shipping and ensure that ►►

the debt incurred to build or acquire each ship will be paid off and the risks to their organisation minimised. Such a strategy is relatively low risk because it insulates the owner from market forces but provides only a modest return on the capital invested and requires a long term view of the economic forces affecting the industry.

For those who have the stomach to take advantage of it, the spot market offers the chance for extraordinary returns when demand skyrockets because of a political crisis, a natural disaster or an arbitrage in the market for the ships the entrepreneur controls. The other side of the coin is that the enterprise's ships can just as easily be unemployable because they are in the wrong place at the wrong time or not capable of handling the cargo which is in demand. In the latter case, the enterprise must have salted away enough in the good times to weather the bad or fail.

Similar factors can be found on the margin of the oil and gas business where independent exploration and production companies bet their enterprise on every rig they lease and well they drill because they rely on leverage to support growth; in the marine construction services sector of that industry where much of the available work tends to be relatively short in duration and longer term contracts are hard to find and generally lower in profitability; and, in the real estate industry where an imbalance between financing costs and available demand can sink a developer who pyramids assets to maximise the leverage achievable by bor-

rowing against existing structures to support new construction or acquisitions.

The high risk and volatility associated with these businesses and the fact that any survivor has stared down failure many times (many successful ship owners were in financial distress before the closing of the Suez Canal during a period of Arab-Israeli discord created an almost instant change in the economics of the tanker market for owners with large crude carriers which did not need to transit the canal to bring their cargoes economically to Europe) means that denial becomes an ingrained fact of life in the face of economic trouble and a miracle is always a real possibility for salvation. In 2004, Hurricane Ivan could be seen as that sort of boon for operators of marine construction and supply vessels in the Gulf of Mexico. A sustained down market in this sector of the off-shore shipping markets achieved sudden reversal and the rejuvenation of company balance sheets because of the destructive force of the hurricane and the need to rebuild and re-supply offshore platforms and oil and gas collecting systems.

As difficult as denial is to overcome in any corporate situation, in these industries senior management is virtually unable internally to acknowledge the possibility, let alone the reality, of failure. Allowing them to delude themselves until the banks and their major suppliers shut them permanently off almost guarantees a liquidation rather than a restructuring. Working with companies in such circumstances requires maintaining closer contact and making common cause

with secured lenders and critical suppliers than would normally be the case. Suppliers and lenders in these industries are also generally less risk averse than traditional lenders and suppliers and more willing to take risks with clients who have proven ability to weather difficulties. As a result the denial stretches well beyond the enterprise and may be sustained beyond the point of no return by suppliers and lenders who lose all room for accommodation by the time they realise and admit the enterprise's true economic situation. The real value of a psychologically adept turnaround and crisis manager in these situations is realised when they are able to affect the opinions and attitudes not just of management but of those few groups to which management will listen. These rarely include the clients' own boards or mid level managers. Senior management believes, because it has done so in the past, that boards which demand turn around help and mid level managers who cry doom are inept and fearful and not to be trusted with the fate of their enterprise.

As counter-intuitive as it is for a turnaround professional to rely on lenders and suppliers for assistance, the willingness and ability to persuade the lenders and key suppliers to put pressure on management early in the development of a crisis can make all the difference to a successful engagement in certain industries. ■

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