A CASE STUDY FROM THE AUTO PARTS INDUSTRY

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Turnaround Corner:

A Case Study from the Auto Parts Industry

A restructuring can seem overwhelming at the onset, especially in the wake of a potential bankruptcy or sale. Patrick Walsh breaks down how a turnaround can be accomplished step by step, showing how even a troubled company can find stability in as little as three months.

By Patrick Walsh

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Working in the capacity of chief restructuring officer for a U.S.-based auto parts manufacturer, Cedar Croft Consulting revised the company's pricing strategy with certain key customers and implemented specific cash conservation measures which allowed the company to win new business and return to profitability.

The Company

The manufacturing company provides services and products to original equipment manufacturers and system integrators servicing the automotive, heavy truck, military, marine and agriculture industries. Operating out of a 120,000 square foot facility in the Southeastern United States, the company specializes in precision tube forming, tube and hose assemblies, CNC machining and value add services. The business was founded in 1987 and acquired by its current private equity owner in 2002. The company expanded and completed a tuck-in acquisition in 2009.

The Situation

Since being acquired by the private equity owner, the company was able to secure several significant contracts in the automotive and heavy truck industries and enjoyed a period of enviable growth and profitability. However, two years prior, the company lost a significant program with a major automotive OEM customer and had not been able to adequately replace this business. Margins in certain product lines were eroding, manufacturing overheads were not being absorbed by the current levels of business and operating losses were consuming availability under existing lender lines of credit.

The management team reacted to the situation by attempting to increase prices across its product lines. These price increases were meeting fierce resistance from key customers, as they were unable to pass these costs onto their own customers in turn, and some were threatening to source products from other vendors. Management had no other plan in place to return the company to profitability.

Cedar Croft Consulting had previously completed several successful engagements for other portfolio companies of this manufacturer’s private equity owner. As a result of that relationship, the company engaged Cedar Croft to assume the oversight of all operations and full cash control of the company, take steps necessary to make changes to the operation, maintain ongoing communication with the key stakeholders, complete an assessment of the company’s business and make recommendations to the shareholder on a going-forward course of action.

The Approach

As Cedar Croft’s president and managing director, I assumed the role of chief restructuring officer. Over the course of three months, our team took the following actions:

We reviewed the company’s financial statements and existing lender arrangements and held discussions with management and staff to learn of its current business processes and going forward strategies.

I met with all sales personnel to understand the impact of recent price increases to all key customers.

The company’s recently implemented customer relationship management (CRM) software was reviewed.

An employment offer to a new sales representative with appropriate industry experience was also assessed.

Discussions were held with several industry-experienced investment bankers to determine the potential value of the company in a sale to a strategic party.

A review of the company's cost structure was completed and a business planning process for the current and following fiscal years were developed. This process included a detailed analysis of profitability by customer.

As with all engagements, Cedar Croft Consulting implemented a weekly communication protocol as an avenue to keep all key stakeholders current with all activities associated with the engagement.

The Engagement's Key Steps

With our reviews completed, Cedar Croft helped craft a plan to get the company back on its feet:

- A 13-week cash flow forecast was prepared, and procedures put in place to update the forecast each week. The forecast highlighted an approaching liquidity crunch.
- Cash conservation policies were developed and implemented to allow the company to manage through a forecasted liquidity crunch.
- Negotiations with key vendors took place to secure their support through the liquidity crunch, including deferring payments for a period of time and negotiating improved pricing for certain product lines.
- Pricing strategies with strategic customers were revised, and meetings were held with these customers to explain how pricing on existing products could be modified in return for partnership opportunities on their new programs.
- The CRM protocols and processes were upgraded to better prioritize and target both existing and potential strategic customers, to track sales backlogs and pipelines and to monitor salespersons' activities and progress.
- A new sales rep was engaged, and we assisted in his onboarding to prioritize the selling approach to his industry contacts in conjunction with the newly developed CRM processes.
- Discussions with industry-experienced investment bankers determined that a sale of the business to a strategic buyer was not an attractive option to the private equity-owner at this time.
- A liquidation analysis was performed to quantify the net recovery to the private equity owner if this option were necessary.
- A review of the company's cost structure determined excess costs in freight and shipping. These were corrected through discussions with existing carriers who agreed to adjust pricing to be more competitive in order to keep the business.

An updated business plan and financial projections for the current and following fiscal years were completed. With these projections, the magnitude of new business and/or cost reductions required to reach profitability were quantified, options for each identified and the probability of success assessed for each.

The Results

The company secured a significant new program from an existing customer that dramatically improved the financial outlook for the business. This was accomplished through meetings and discussions with the customer, explaining the rationale for the recent management-imposed price increases and agreeing to roll back the price increases in return for new business. The excess capacity in the plant allowed the company to easily take on this new business.

Continued business with another key customer was secured for an additional year after the customer had threatened to leave because of the recent price increases. After analyzing the net profitability of this customer's business and the impact of losing them, revised pricing and timing of implementation of the increases were negotiated that were acceptable to both parties.

The company returned to profitability within three months of the CRO's engagement with the cash management protocols in place and without the need for additional financing or investment from the private equity owner. This convinced the owner to discard the notion of a sale, and to support the company in executing its business plan for the next two years.

In Summary

Careful customer intervention was a key success factor in this engagement. With management informing customers of the price increase prior to the CRO's engagement, relationships with key customers were tenuous at best. An analysis of profitability was critical in establishing a strategy on how to best approach each key customer and in turning a potential loss of desirable business into a win-win for both parties.

Patrick Walsh is the president and managing director of Cedar Croft Consulting and has provided clients, throughout a variety of industries, with turnaround and crisis management, financial advisory, cash flow management and profit improvement services for over 20 years. He earned his Certified Turnaround Professional designation from the Turnaround Management Association in 2005 and holds two accounting designations.

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Panelists*: Judge Kevin J. Carey, District of DE
Steven Mitnick, Partner, SM Law
Patrick Walsh, President,
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