

Middle Market Lessons from General Motors' 39 Days in Bankruptcy

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It sounds incredible. General Motors Corporation filed for bankruptcy on June 1, 2009 and on July 10, 2009 its core assets were sold in what has to be one of the largest—if not the largest—363 bankruptcy sales of all time. 39 days. This is remarkable because most Chapter 11 cases take more than a year to be resolved. Through this process, old GM is dead and new GM (General Motors Company) has a chance to emerge with a more viable business model. Focusing strictly on GM's bankruptcy case, we can learn some valuable lessons about how planning and focused decision making can turn a terrible situation into something more palatable. We should view the case as a great example of the possibilities for reviving an insolvent business.

Our economy is struggling and the absence of the worst news is considered great. The *Wall Street Journal* reported on August 1 that the United States economy has pulled out of its tailspin. The news which sparked this encouraging headline was the report that the GDP contracted at a 1% rate in the second quarter. This is significant because the rate of contraction has slowed considerably from 6.4% in Q109 and 5.4% in Q408. On August 5, ADP reported that the pace of new unemployment claims may be slowing. But, our economic recovery is just beginning and we likely have many months of unease ahead.

While commentators debate whether the recovery will come in the form of a U, V, or W, there is consensus that the recovery is a 2010 event. If this plays out, businesses that are waiting for a rising tide to lift them will have to survive nearly another year. Waiting and hoping for the best is not an optimal strategy. Without a backup plan, businesses lose control and are forced into liquidation. To avoid this outcome, all companies should take a page from the playbook of GM's distressed team: objectively evaluate the basic business model and prepare to execute on plans that will allow the core business to survive. This is particularly important for lower and middle market companies. GM had the luxury of being too big to fail. GM lost about \$30 billion in 2008 and the U.S. Government provided approximately \$50 billion in financial aid. Most struggling businesses will not be so lucky because there is little credit available and many private investors seem to be waiting. The best businesses will adjust their operations to fit the new norm.

All businesses should assess their competitive position immediately and determine whether distress, should it come, would be in the form of financial distress or economic

distress. If your company has a viable business model but is having difficulty maintaining positive cash flow, its distress is financial. Companies in financial distress can use traditional tools for restructuring to insure future viability. Companies whose basic business model is flawed face economic distress. Companies in economic distress have insufficient operating margins to be viable and they should be closed down. All management teams should make this determination objectively and immediately.

There are many tools commonly used to make objective operational assessments. For example, undertake a "SWOT" analysis: assesses your strengths, weaknesses, opportunities and threats. A perceptive manager can use this information to determine whether the business has a defensible market opportunity. A component in this analysis is to determine the company's operating margins, product by product and business unit by business unit. Another tool is to prepare an accurate rolling cash flow projection. This will help the company manage its cash and help managers prioritize their initiatives so as not to exceed the cash available. Finally, all business managers should identify all of the key drivers of their business and measure the productivity of each element. For example, sales performance should be measured by an objective scale such as the number of profitable sales booked relative to the number of sales calls made. With the right data, the best management teams and owners can take action.

All constituents in corporate management and ownership--business managers, investors, creditors and lenders--need to get ahead of the coming wave of issues and maximize their chances for survival. Assessing the fundamentals of each business will provide the data necessary for effective decision making. There is no room for guesswork in today's environment.

Large companies have the luxury of scale and, with GM as an extreme example, their constituents can compromise significant issues in order not to suffer what would be a much larger loss if the company fails. Smaller companies may face more intractable constituents and need to be very focused on what they do well. There are fewer "white knights" focusing on the lower and middle market. The distressed investment community is looking for opportunities up-market because the opportunities are plentiful and more profitable. Most investors will not consider looking down-market until the supply of upper market opportunities diminishes.

The best businesses adapt to their environment. Middle market business managers and stakeholders must assess their positions immediately and adapt to maximize their chances for survival. To do this, middle market companies need to take a page from GM's distressed transition playbook and get ahead of the curve.

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