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## Get Into Gear ... Process Improvement to Generate Cash for Brick-and-Mortar Industries

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Date: Mar 06, 2013 @ 07:00 AM

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Since the credit crisis of 2008, the world of restructuring and turnarounds, especially in traditional brick-and-mortar industries like manufacturing and distribution, has changed dramatically. Due to tighter lending rules, there seem to be fewer opportunities to attract refinancing and, as a result, if the "problem" loan is not kicked down the road, the path to liquidation becomes an impending reality. In some situations collateral asset devaluations because of changes in the market value of fixed assets, inventory write downs, and/or major customer bad debts can force a lender into an over-advanced position. The lending institution is then faced with an even shorter period of time to make a lending decision. Funding decisions that, in the past, might have been made for months are now being made for weeks or even days. As professional consultants brought in at the lender's insistence and working for the debtor, restructuring advisors have had to pick up the pace and deal with the issues of cash flow, entity viability, and organizational adjustment in a shorter period of time and often with fewer resources.



### Get Liquid

It becomes imperative, therefore, that all of the debtor's assets are brought into play as rapidly as possible. In addition to speeding up collections, reducing inventory, selling non-core assets, and slowing outgoing payments there also other, less obvious ways to generate cash. Innovation becomes the order of the day and the search for more liquidity needs to get underway quickly.

One of the best methods to generate immediate cash is the elimination of *waste*. Waste is present in any activity that does not add value to the company's product or service. A "Lean" approach to dealing with all operations can yield benefits of reduced investments in working capital, smaller payroll requirements, and the elimination of excess costs and expenses. Lean and Six Sigma are the most widely used process-improvement approaches practiced today, and can be combined into an approach we call LeanSigma. By maximizing productivity and efficiency this approach has saved companies millions of dollars across manufacturing, services, distribution and back-office processes, developing an accelerated approach which creates value rapidly and with minimal capital investment by focusing on speed, sustainability and continuous improvement.

Money that is not spent on waste becomes available to reduce leverage, eliminate losses and increase the overall morale and the output efficiency of the organization generating increased customer satisfaction. Lean efforts have traditionally been seen as change activities that take many months to implement, since a change in culture is a key part of a lean transformation. In a "distressed" environment, however, the drive for change is already there, and so culture can change quickly as we work together to eliminate waste and re-design how work is performed.

Often there are a host of issues that cause companies to restructure. One of the most common is an over-leveraged financial position stemming from losses, or cash drains from overdue accounts receivable, excess inventory or non-core investments. These issues are exacerbated when extra cash is needed to support factories that are poorly configured, forcing extra labor costs to re-transport goods, or production that is interrupted by the lack of synchronous interaction within the supply chain. Such challenges mushroom, creating the need for back-up inventory, causing obsolescence, damaged goods, capacity constraints and other unnecessary spending. Eliminating the waste of non-value added activities addresses unnecessary costs and excess investments, reducing losses that contribute to increased and unsustainable leverage.

### Get Started

The first step in eliminating waste in any organization is an assessment of the state of the business. This requires a deep dive into the components of the Cost of Goods. An overall understanding of the material costs, inbound and outbound transportation costs, labor, and production trends

provides a solid basis for exploring opportunities for savings. In order to identify the potential benefit of curtailing or consolidating activities in manufacturing and distribution businesses, it is necessary to have a clear delineation between direct and indirect costs.

In distressed situations time is working against you. Finding the low-hanging fruit that provides the highest return for the least cost needs to happen fast. Inquiries into the manufacturing process as to quality capability and scrap issues, material flow and work-in-process levels, cycle times, capacity issues and bottleneck operations can quickly reveal relatively large opportunities for improvement. Inbound and outbound transportation costs are often overlooked or not well understood. Freight terms are a critical component, and combined with re-sourcing efforts, represent savings in the 10-15% range. Warehousing efficiency is another opportunity for waste reduction. Medium- to longer-term looks at the overall manufacturing and distribution network design typically add another 5-10% in savings. All of these improvements have a direct impact, freeing up cash and relieving pressure on liquidity. Best of all, transportation savings can be implemented in 60-90 days.

External relationships between the company and its suppliers, service providers, and customers are also areas of prime importance when identifying the extra costs of waste. When was the last look at re-sourcing initiatives for direct materials and transportation costs? Often, because of the late delivery, poor quality, and interrupted services that are a result of liquidity constraints, these relations are strained. Assessing everything from the perspective of value-added versus non-value-added activities creates a roadmap for change.

### **Get Focused**

It is important to establish early on a long-term view based upon right-sizing the business. All corrective actions should be done with that view in mind. For example, if the goal is to reduce the bank debt for a distribution company, it could be a bad idea for the sales force to add customers in outlying areas. Of course, new sales are generally good but, this outcome could increase the leverage, and add complexity to customer satisfaction issues, which in turn can put further strain on areas of the organization that need simplification. Look to concentrate routes and consolidate activities. The art of management is to align the goals of the employees with those of the organization.

The lifeblood of a business is a profitable customer. That is why it is imperative to take a hard look at customer satisfaction issues. Search for the bad news. Every unresolved customer issue adds waste to the system. Protect the profitable customers at all costs and convert or fire unprofitable customers.

Stabilizing cash-flow by matching material purchases to sales can be accomplished using supply-chain evaluation techniques to squeeze out the waste and increase turnover. Enlist the supply base in the attempt to take extra costs out of the system. In manufacturing operations, the efficient flow of material has a significant effect on the ability to reduce waste on the factory floor and eliminate excess inventory. When raw materials flow in the door in the same pattern as shipments flow out the door, cash generated from collections match the cash requirements of the suppliers resulting in a more stable environment even in cash-starved businesses.

### **Get Moving**

Wherever possible, it is important to begin to measure everything and identify all costs associated with activities. Build a data base and knowledge-share with all the employees. Post charts of Key Performance Indicators. Let all concerned know what is important and that there is accountability. Create momentum. Go for small wins to set the pace. Stay focused and reward feedback.

One of the first challenges is to get everyone on the same page. Research shows that participative management is the most effective way to stimulate ideas and involvement. That is an environment in which impediments can be removed and employee enthusiasm can flourish. Enlist the help of influential leaders to help guide the process. Be aware that an influential leader it may turn out to be on the line, not necessarily the lead manager or executive in the area.

Work closely with the line employees and help them identify the waste in excess motion, waiting time, excess inventory, excess time to set up and break down operations. Inquire as to the efficiency of all machinery and equipment. Analyze the maintenance and other support costs of capital items including transportation and other equipment.

Change is the one sure thing that needs to happen to address the reduction of waste in the restructuring environment. The major impediment to instituting change and identifying and correcting waste issues is entrenched management. On occasion (more often than not) we deal with inbred management with disparate objectives. A typical symptom of this is the lack of good corporate communication and little meaningful feedback. Often we will see power concentrated in a few executives with built-in bottlenecks in the delegation of authority. This creates inertia, sacred cows and other barriers to success. Organizations need to be flexible to deal with the ever-changing environment.

### **Get Real**

The purpose of an organization in a business is to bring complementary skills together to achieve the goal of making a profit, not to perpetuate itself. In distressed situations that require restructuring, this notion needs to be communicated repeatedly to employees in order to maintain morale. Management and employees must be equipped with the tools they need to sustain short-term improvements, and the culture must support corrective action day-in and day-out—it must be an engine for continuous improvement. These are the ingredients that will make the search for waste in the system pay off, and generate the cash needed to survive and thrive. Establishing realistic goals and achieving or exceeding them provides the impetus to continue on the path to recovery. It also allows third party lenders and/or investors to get on board and work with the organization rather than against it.

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Stephan M. Pinsly, managing director, is a veteran chief financial officer and chief operating officer of public and privately-owned middle market corporations, providing strategic turnaround leadership for 30 years. He has accumulated a wealth of experience in solving intricate, difficult debt re-financings and complex business viability issues. His industry expertise



spans across many business types – from distribution, manufacturing, services and retailing companies – and includes pharmaceuticals, auto parts, telecom, sporting goods, jewelry, and marine supply and repair.

Pinsly began his career at Price Waterhouse & Co. after receiving a bachelor’s degree in accounting from Queens College, CUNY. Following that, as an entrepreneur in a private investment firm, he participated in transactions related to the acquisition and disposition of distressed companies. Prior to joining Getzler Henrich he served four years as a director and senior vice president of a regional middle market turnaround management consulting firm. Pinsly is a certified turnaround professional and a certified public accountant. He is a member of the Turnaround Management Association as well as the American Institute of Certified Public Accountants and the New York State Society of Certified Public Accountants.

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