10-13-2010

Help for Businesses in Tough Economic Times

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Hubris born of success

Among Collins’ examples to explain the first stage of decline is Motorola. Motorola, formerly known as Galvin Manufacturing Corporation, was able to envision carrier tactics on carrier into the future almost 10 years. However, they dismissed the digital revolution.

Motorola used heavy-handed tactics on carrier companies, such as Bell Atlantic, which challenged Motorola executives. Motorola was showing the first signs of Hubris: arrogance. Basically, Motorola’s employee numbers fell from 147,000 in 2001 to 88,000 in 2003. Motorola’s stock fell more than 50 percent from 1995 to 2005. The markers for Stage 1 are “success entitlement, arrogance; neglect of primary flywheel; what replaces ‘vision’ is ‘a brick in learning orientation’” (pp. 43–44).

Undisciplined pursuit of more

Collins uses Rubbermaid as one example. Over a three-year span, Rubbermaid introduced 1,000 new products. The company had to grapple with covering manufacturing costs and filling orders on time, and then it began to crack. The company eliminated approximately 6,000 product variations and 1,170 jobs and sold out to Newell Corporation in 1998. The markers for Stage 2 are “unsustainable quest for growth, confusing big with great; undisciplined discontinuous leaps; declining proportion of right people in key seats; easy cash erodes cost discipline; bureaucracy subverts discipline; and problematic succession of power” (pp. 63–64).

Denial of risk and peril

Motorola, on a quest to make an “anywhere-on-Earth connection available to people everywhere” (p. 66), developed Iridium, a hand-set phone that was the size of a brick that worked only outside. In 1991, the Iridium project became a separate company with Motorola as the primary stockholder; Iridium launched in 1998. Motorola handsets cost $3,000 and calls cost between $3 and $7 per minute. In 1999, Iridium filed for bankruptcy and defaulted on $1.5 billion in loans. Collins says “any deterioration in gross margins, current ratio, or debt-to-equity ratio indicates an impending storm” (p. 79). The markers for Stage 3 are “amplify the positive, discount the negative; big bets and bold goals with empirical validation; incurring huge downside risk based on ambiguous data; erosion of healthy team dynamics; obsessive reorganizations; and imperious detachment” (pp. 81–82).

Grasping for salvation

When a company begins looking for a silver bullet, Stage 4 begins. Jim Collins gives examples such as “betting big on an unproven technology, pinning hopes on an untested strategy, relying upon the success of a splashy new product, seeking a ‘game changing’ acquisition, attempting to turn an image makeover, hiring consultants who promise salvation, seeking a savior CEO, expounding the rhetoric of ‘revolution,’ or in its very late stages, grasping for a financial rescue or bailout” (p. 89).

A company can grasp for a brief improvement, but the results don’t last. The markers for Stage 4 are “a series of silver bullets; grasping for a Leader-as Savior; panic and haste; radical change and ‘revolution’ with fanfare; hype precedes results; initial upwelling followed by disappointments; confusion and cynicism; and chronic restructuring and erosion of financial strength” (pp. 100–101).

Capitulation to irrelevance or death

In Stage 5, “Cash tightens. Hope fades. Options narrow” (p. 105). Jim Collins uses Zenith as an example of a company that went through all five stages of decline. Later, Collins gives an example of Xerox.

When Anne Mulcahy became Xerox’s chief executive, Xerox was in Stage 4 of decline. In early 2000, Xerox posted losses, but by 2006 the company was growing again.

Mulcahy “used decline as a catalyst” (p. 110). Collins says, “As long as you never get entirely knocked out of the game, there remains always hope” (p. 120).

Appendices

In Appendix 6, he gives three examples of decline and recovery: IBM, Nucor and Nordstrom. Overall, Collins has overwhelmingly good examples, good advice and good research to help businesses in these tough financial times.

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In a recent decision handed down by the Eleventh Circuit Court of Appeals in March, a vendor dealing with a company operating in Chapter 11 was ordered to give back almost $2 million in payments on post-bankruptcy invoices. The reason: Unbeknownst to the vendor, the debtor did not have authority to expend its cash. When considering business transactions with companies operating within bankruptcy proceedings, it is essential to protect yourself from a similar situation that can result in significant losses.

When an operating business files for Chapter 11 bankruptcy protection, vendors and others who do business with the debtor post-filing are given the protected status of “administrative expense claims.” They have a priority over pre-bankruptcy claims. The bankruptcy court code gives vendors this favored treatment in order to encourage them to do business with debtors in bankruptcy.

Chapter 11 debtors are expected to pay their post-bankruptcy bills on a current basis as a condition of being allowed to use the bankruptcy process to restructure their affairs. If the debtor fails to pay the vendor or creditor, they can seek payment by court order for the Chapter 11 “administrative expense.” As a result, people doing business with companies operating in Chapter 11 believe they are protected, and in many ways this is true. However, the bankruptcy court also grants protections to a Chapter 11 debtor’s secured lenders.

Cash, deposit accounts, securities and negotiable instruments pledged as collateral for loans, as well as cash proceeds of other collateral such as inventory and receivables, constitutes “cash collateral” under the bankruptcy laws.

A debtor may not use or spend cash collateral unless the lender consents or the court enters an order upon a finding that the lender’s interests are adequately protected.

In the case of In re Delco Oil, the debtor was paying its vendors with funds that constituted cash collateral, but it did not have a court order or a stipulation. In fact, the lenders were objecting and the bankruptcy court denied the debtor’s motion for leave to use cash collateral. The vendors were ordered to return the payments they received, even though they were unaware the debtor did not have authority to use cash collateral.

As a result, vendors transacting business with companies in Chapter 11 need to take the initiative and ask for assurances the debtor has authority to use and spend its cash.

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