

How to Restructure A Defense Contractor. Turnaround Corner: Inside the Country's Top Turnaround Firms

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Successful Restructurings Magazine, published a Special Interview of Interest About John M. Collard, turnaround specialist and equity investor.

John Collard On: How to Restructure A Defense Contractor

Turnaround Corner
Inside the Country's Top Turnaround Firms

By Donna J. Tuttle

On the surface, development of weapons systems has little to do with environmental impact studies. But turnaround manager, John M. Collard, president of Annapolis, Md. based, Strategic Management Partners, Inc., recently found a way to link the two and thereby save his client, a high tech weapons system defense contractor, from financial suicide. Now, instead of analyzing the trajectory power of jets and missiles, the firm studies the movement of pollution particles through the air.

Collard's client, who must remain anonymous due to a client confidentiality agreement, is a 300 employee firm with \$33 million in annual sales. Before Collard became involved, the company developed and deployed weapons systems for the government. Its major customers included air and space divisions of major governmental agencies such as the Strategic Defense Initiative (SDI), the National Aeronautics and Space Administration (NASA), and the U.S. Air Force. [Today the firm has grown six-fold]

Much of the firm's work involved simulation modeling, a type of computer programming that recreates events like missile launchings and jet takeoffs in true to life fashion. Using the sophisticated programs, the firm's employees measured different characteristics of flight and movement.

Simulation modeling was profitable for the company during the '80's. However, the '90's brought defense cutbacks, the end of the Cold War and a change of administration. There was little need for such "War Games." As a result, the company's narrow specialty hung like a noose around its neck.

When Collard walked in the firm's doors, annual sales had dropped from \$42 million to \$33 million, the company hadn't won a major contract in three years and its market was shrinking rapidly. As the

company's profit margins became smaller, it increased its bidding prices -- making it even less competitive in contests for major contracts.

In assessing the firm, Collard, who specializes in defense conversion, pinpointed two other signs of trouble common to ailing defense contractors. First, the company's backlog of contracts was eroding.

"In federal contracting circles, companies live by their backlog," Collard said. "For example, say the company wins a five year, \$10 million contract. The first year into the contract, it may only have been paid \$2 million. That means the firm still has an \$8 million backlog."

Second, the company's bid and proposal (B&P) fund, the pool of money it uses to research and prepare bid proposals for new contracts, was deteriorating. "Not only was the company coming to the end of its rope on old contracts, it also had limited funds to go out and get new ones," Collard said.

Collard and management spent the majority of their time trying to pinpoint a service or product that could project the company into the commercial market. The company finally realized its core strength was measuring the movement of objects through space • but those objects didn't have to be defense related.

Collard suggested his client try to cash in on the environmental boom. "I figured they could analyze how particles of pollution float and move through the air. They told me I was crazy. After meetings with the Environmental Protection Agency (EPA) and some review of upcoming legislation, the company started to realize that maybe I wasn't crazy," Collard said.

Within the first six months of applying its expertise to the environmental industry, Collard's client won three major contracts. Today, its possibilities seem endless. The company can go after contracts to identify radiation levels coming from nuclear reactor chimneys; contracts to measure the forces of weather patterns; and contracts to examine the movement of acid rain particles. And with the flood of EPA legislation requiring commercial business to identify and measure the pollutions they generate, the company's fortunes seem secure.

While company turnarounds in other industries almost always call for a restructuring of the balance sheet, that is not the case in the defense or federal contracting industry.

"In most every turnaround case, crisis managers say 'Restructure the balance sheet. Lay off people,'" Collard said. "Those tactics don't work in the defense contractor industry. With defense contractors, there usually are not a lot of assets. Their balance sheet is not very complicated. Usually, they rent a place and hire lots of people, but they don't have a lot of debt or suppliers. So the main step in converting them to new marketplaces is to build a strong selling function."

Once Collard helped this weapons systems client build a selling function and identify a new market, there was no need to retool • the firm continued to use its old equipment. Collard then consolidated seven of the firm's divisions into three including one that now deals with government testing and evaluation, one that performs studies and research and one that is developing the environmental aspect of the firm, which management believes will eventually account for about 50 percent of the firm's

business.

What follows are Collard's recommendations to crisis managers with clients in the defense contracting or federal contracting industry.

Put a sales force in place.

"Many defense companies and federal contractors don't have a sales force," Collard said. "In government contracting, commissioned salespeople are not an allowable cost. Firms are so used to responding to requests for proposals (RFPs). To survive in the commercial market, companies must build a strong selling function."

Use subcontractors to meet employment needs of big contracts.

"Many defense firms get into this almost chicken and egg scenario... They wonder how they can win big contracts without having a large employment pool; then they worry if they can afford the employees if they don't get the contract," Collard said. "By forming alliances with subcontractors, companies can keep their personnel costs down. While many firms hate to give part of the contract money away to subcontractors, they really are saving money because they're not paying annual salaries and overhead costs for that many permanent employees."

Put a Bid Information Review (BIR) process in place.

"The salespeople don't always ask the hard questions," Collard said. "The BIR process is structured with between 40 and 100 questions that force the salespeople to ask specifics of the company/agency seeking contractors. Often the best thing the BIR can do is let the company know if the contract isn't a good match for it. It also helps salespeople get a real feel for what the company issuing the contract really wants. From that, they can figure out how to differentiate from the others who are bidding."

Look beyond the company's major product for new sources of revenue.

"Most people limit their thinking and assume they have to deliver the same product in the same way to a new marketplace," Collard said. "If the company makes airplanes for the defense industry and suddenly finds that with defense cutbacks, a shrinking commercial market and limited global market, they think they're doomed. Often, they're not. They have subcomponents of that airplane that are very marketable • guidance systems, fuel systems, tracking systems, electronic systems. They just have to study new markets and applications."

For example, Collard said, one of his clients worked in the military specifications field • an area that requires high tolerance equipment with a low margin for error • like the Hubble Space Telescope. Faced with financial difficulties, the company didn't know where to look for new markets. Collard suggested that they work at a lesser tolerance level • making products that were high tech, but that didn't necessarily meet military specifications. "Then there's less spoilage. It doesn't take as much time. The cost goes down. And the company is able to compete elsewhere."

Review the company's old bid files.

"Firms spend millions of dollars developing and researching technology to meet bid specifications," Collard said. "Then, if they don't get the bid, they forget about their work. Maybe the piece of technology wasn't fast enough or accurate enough for that particular bid, but it may have application in the commercial market.

Sometimes It's Who You Know That Counts

The conversion to a peace time economy is forcing many companies into a battle for increased sales, said John M. Collard, an Annapolis, Md. turnaround specialist. Many defense contractors and firms think they can simply jump into the commercial or international markets without changing the way they do business. That, Collard said, usually is fatal. He continued "You must often change the culture of your company to be successful in new markets."

"In the commercial market, you may be providing exactly what the buyer needs, but the buyer may suddenly decide he or she doesn't like your tie. And by the way, one of your competitors may have a similar, yet inferior product, but it's starting to look better than yours because your competitor has had the buyer out on the golf course," Collard said.

Collard's advice: Relationships mean everything in the commercial market, and they are maintenance-intensive. "Performance under pressure is the key to survival here," he said.

Reference:

[Library: John Collard On: How to Restructure A Defense Contractor](#)

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About Collard

John M. Collard, is Chairman of Annapolis, Maryland-based Strategic Management Partners, Inc. (410-263-9100, www.StrategicMgtPartners.com), a nationally recognized turnaround management firm specializing in interim executive leadership, asset recovery, and investing in underperforming companies. He is Past Chairman of the Turnaround Management Association, a Certified Turnaround Professional, and brings 35 years senior operating leadership, \$85M asset recovery, 40+ transactions worth \$780M+, and \$80M fund management expertise to run troubled companies, and advise company boards, litigators, institutional and private equity investors.

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