

## CORPORATE TURNAROUNDS AND VALUE CREATION

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## Outline

1. My experiences with turnaround situations and shareholder value creation:
  - Chrysler
  - IBM
  - Apple
  - Tyco International
2. Summary – The key elements for a successful turnaround

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## What Produces Restructuring Situations?

### *The Symptoms:*

- Wrong Strategy?
- Wrong Business Model?
- Poor Execution?

## What Produces Restructuring Situations?

### *The Disease:*

- Poor Governance?
- Inadequate Management?
- Major Shift in Industry Conditions?

## Chrysler Corporation

- Great Strategy:
  - ~ Invented the Minivan
  - ~ Bought Jeep early in the SUV revolution
- Business Model Too Slow and Costly:
  - ~ Major changes to the product development process
  - ~ Major reductions in administrative costs (aka bureaucracy)
- Operations Seriously Deficient in Passenger Cars:
  - ~ Huge progress by Ford and the Japanese

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## IBM Corporation

- Broken Strategy:
  - ~ Premium prices way too long
  - ~ Decentralization to a fault
- Business Model Too Slow and Costly:
  - ~ Bureaucracy precluded competing in short cycle businesses
  - ~ SG&A + R&D \$7 Billion (25%) too high
- Operations Seriously Antiquated in Many Areas:
  - ~ Go-to-market, procurement, finance, product development, even IT!

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## Apple, Inc.

- No Strategy:
  - ~ Key R&D resources being squandered on Newton
  - ~ No plan to conquest Microsoft customers
- Business Model:
  - ~ Serious distribution issues
  - ~ Losing dominance in education to Dell
- Operations Reasonably Decent, But:
  - ~ Too much manufacturing in North America rather than Asia

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## Tyco International, Ltd.

- Single-Legged Strategy:
  - ~ Acquisition Machine
- Business Model Had Excessive Balance Sheet Leverage:
  - ~ Anything going wrong could result in a financial crisis
  - ~ Accounting approaches very aggressive
- Operations Essentially Not a Priority:
  - ~ Hundreds of acquisitions with no “back office” or manufacturing consolidation



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## What Are the Similarities/Dissimilarities?

### *The Symptoms*

	Strategy	Business Model	Operations
Chrysler	Overall Good	Too Slow & Costly	Left Behind in Cars
IBM	Severely Flawed	Too Slow & Costly	Behind Except in Mainframes
Apple	Essentially None	Distribution Problems	Mfg. Footprint Issues
Tyco	Good but Risky	Too Costly	Largely Sub-Par
<b>Similarities:</b>	<b>2 of 4</b>	<b>3 of 4</b>	<b>2 of 4</b>

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## What Are the Similarities/Dissimilarities?

### *The Disease*

	Governance	Management	Industry Conditions
Chrysler	Independent, Strong Board	Lack of Good Teamwork	Japanese Competition
IBM	Strong Board, Decisive	Rigidity to Past	Titanic Industry Changes
Apple	Silicon Valley Vets, but...	Lack of "Mac Passion"	Microsoft Domination
Tyco	Hampered; in Awe of CEO	Acquisition Machine	Largely Well-positioned
Similarities:	2 of 4	3.5 of 4	2.5 of 4

## Chrysler Turnaround Results

- Initial Results:
  - ~ Spectacular. Share price from low of \$9 in 1990 to \$45 in 1993 when turnaround “completed”
  - ~ Chrysler purchased by Daimler-Benz in 1998 for \$35 billion
- Longer Term Results:
  - ~ Major restructuring II in 2002 to 2004 period
  - ~ Major restructuring III commenced in 2006
- Conclusions:
  - ~ Fundamental competitive weakness versus the Asian producers never adequately addressed

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## IBM Turnaround Results

- Initial Results:
  - ~ Spectacular. Share price from low of \$10 in 1993 to \$124 currently
- Longer Term Results:
  - ~ Company has continuously transformed itself, growing its services and software businesses, and shrinking its hardware businesses
  - ~ It has not let "success" preclude it from taking periodic retrenchment actions where needed
- Conclusions:
  - ~ Growth in the services industry is slowing... Could indicate additional restructuring to come

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## Apple Turnaround Results

- Initial Results:
  - ~ Spectacular. Share price from low of \$4 in 1997 to \$20 in 2000, and now at \$168
  - ~ Principal initiatives were award-winning designs and substantially improved Mac operating system
- Longer Term Results:
  - ~ Apple has invested in two huge initiatives, both highly successful:
    - Its own B&M distribution – key to expanding Mac platform sales
    - The music business, a transforming event for the music industry
- Conclusions:
  - ~ Continual innovation--the latest being the iPhone

## Tyco Turnaround Results

- Initial Results:
  - ~ Spectacular. Share price from low of \$9 in 2002 to \$47 currently
  - ~ Multiple crises successfully addressed:
    - Board and management credibility
    - Accounting and liquidity crises
    - Legal and regulatory crises
- Longer Term Results:
  - ~ Acquisition machine turned off; focus shifted to organic growth and operational excellence
  - ~ Decision made that best way to maximize shareholder value is to break up the company
- Conclusions:
  - ~ Separation of \$40 billion Tyco into three pieces should allow each new company to better focus

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## Key Turnaround Elements (in my experience)

1. Senior management passion and determination
2. Sell, sell, sell, explain, explain, explain it to the troops
3. Set the example. “Tone setters” are important
4. Benchmark everything
5. Take a highly structured approach
6. Measure and report status frequently

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## Role of Board of Directors (Governance) in Situations Requiring Turnaround

- IBM:
  - ~ After three years of precipitous deterioration, the board took drastic action; new CEO and CFO appointed from outside the industry
- Chrysler:
  - ~ One can conclude board wanted new CEO, but wanted an “orderly transition”
- Apple:
  - ~ After two straight underperforming CEOs, board approached Steve Jobs to return, which he agreed to do subject to major changes in board composition
- Tyco:
  - ~ Severe regulatory and legal situation forced the prior board to go outside for new CEO, and dictated major change in board composition



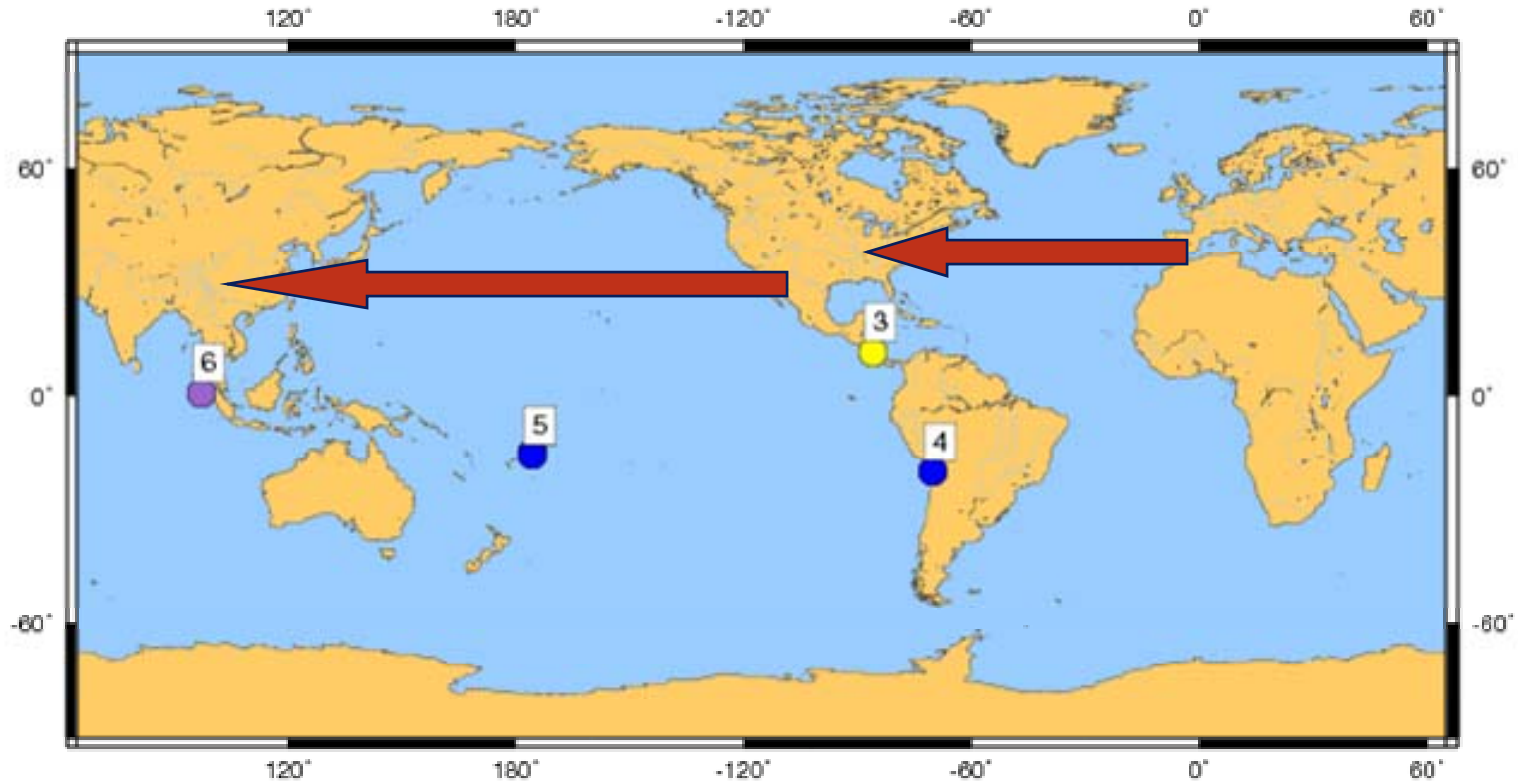
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## Wrap-Up

- The World is Changing Rapidly
  1. Shifting Demographics
  2. Emergence of China with others not far behind
  3. Global Warming
  4. Transformation of American Business
- Steady-State is No Longer the Norm (if it ever really was)
- Turnarounds are Crucial Where Needed, But....
  1. Cannot be considered to be “one time” events
  2. Must be followed by continuous improvement approaches, and high levels of strategic adaptability
  3. Global competition is here to stay even if the lobbyists, politicians, etc., try to stop it. Capital will flow to where it gets the best returns.

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## Economic Center of Gravity of the World



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## Sovereign Wealth Funds

### US Investment Activities:

Citigroup / Merrill Lynch / Morgan Stanley / Others

\$21.5 Billion Invested in US in 2007 [A]

\$22.6 Billion Invested in US in 2008 [A]

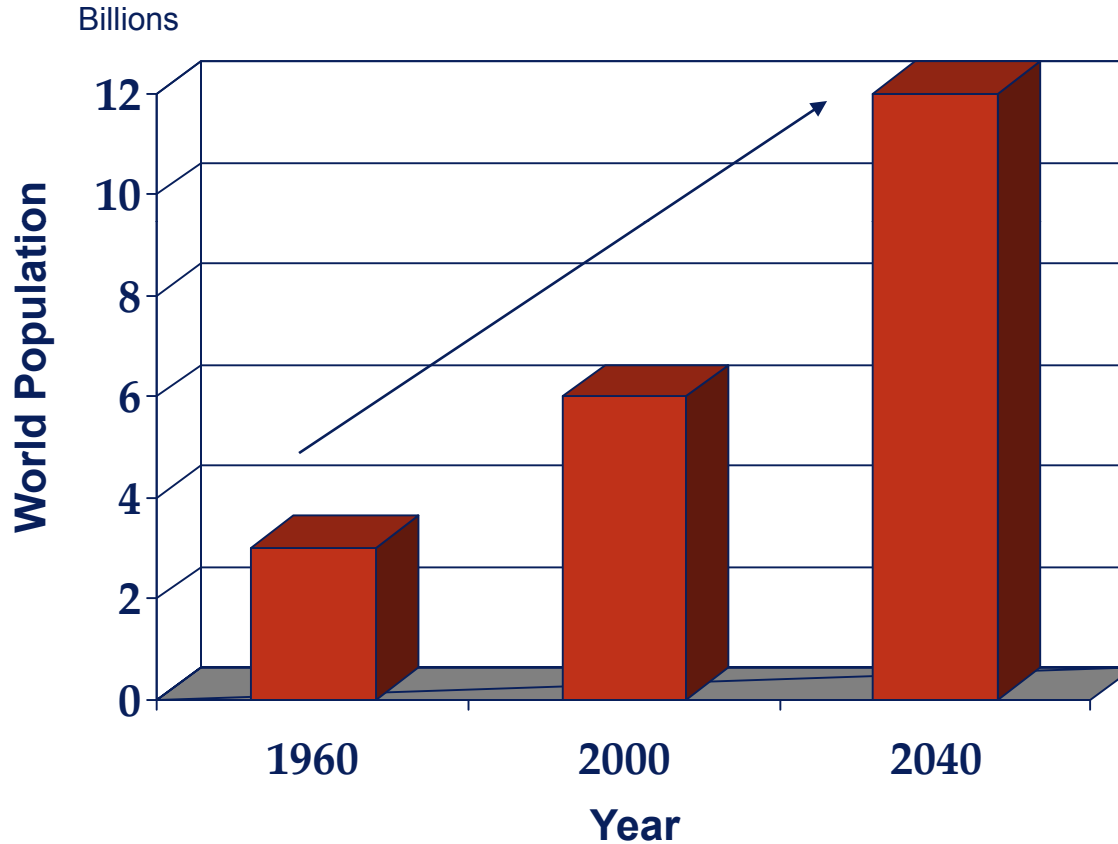
<u>Net Capital Outflows [B]:</u>	<u>\$(Billions)</u>		
	<u>1995</u>	<u>2000</u>	<u>2006</u>
Oil Exporting Countries	35	192	484
Eastern Asia	133	198	446
Rest of World	114	119	389
Total	282	509	1,319

[A] Source: Wall Street Journal / Thompson Financial.

[B] Source: McKinsey Global Institute.

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## Global Warming...AKA Global Crowding



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