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COVID-19 Response: The Operations Lever in Your Playbook

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The COVID-19 crisis has created a difficult and unique set of financial and operational challenges for middle market companies across industries. In a few sectors, new sources of demand have created bright spots. But for most, it's a different situation, one of steeply declining or volatile demand coupled with a highly uncertain duration and rebound path. This unique situation requires a unique response to successfully manage solvency and profitability.

We see most PE-backed companies moving quickly to action with an effective *finance-driven* cash management playbook. Short term cash flow projections are built to gain detailed visibility into sources and uses of cash. Control of non-essential cash outflow and preservation of inflow sources is quickly locked down through a closely managed communication process with key stakeholders; and resources are assigned to focus on immediate management of A/R and A/P.

However, for companies that market, manufacture, or distribute tangible products, the current environment also creates a unique set of operations-driven opportunities to improve cash flow and profit margin in the near term. While these operational opportunities are not usually as visible as the quick cash management levers outlined above, the financial impact can be significantly greater.

We offer a few additions to your restructuring playbook to align your company's *operations* with the realities of the current market and drive the response that the current crisis demands: 1) Getting quick control of cash; 2) Stabilizing the supply chain; 3) Restructuring targeted elements of the value chain with the longest levers on cash flow; and 4) Maintaining credibility with stakeholders including employees, customers, key suppliers, and lenders.

1. **Quickly control cash**

   Suggested actions:

   - **Launch internal communications** to reorient employee behavior around the new mindset
   - **Negotiate extended payment terms** with your larger suppliers
   - **Put controls in place for placement and timing of P.O.s**
   - **Reset forecasting and inventory algorithms** to align with new demand projections, reducing excess working capital tied up in inventory

2. **Stabilize the supply chain**

   Suggested actions:

- **Secure sources of material and component supply.** Supply chain disruption has spread across sources in almost all manufacturing centers across the globe. Check critical supplier health and production locations at all levels in the supply chain, and develop contingency plan details at the tactical or daily level
- **Proactively negotiate with key vendors to ensure stabilized supply in the near term** – your suppliers are as worried about you as you are about your customers
- **Place extra emphasis on effective Sales, Inventory, and Operations Planning (SIOP) processes** to control service levels and EBITDA as demand volatility and resource constraints set in
- **Review and de-risk your extended supply chain**. Develop safety net options through dual souring strategies, and act now – competitors and companies in adjacent industries will quickly consume capacity as they diversify operations in other low-cost supply regions

3. Refocus or restructure targeted elements of the value chain

Suggested actions:

- **Resist the temptation to focus only on "quick hits"**. Look beyond the obvious cost levers, as facility and supply chain network fixed-cost rationalization can be the most powerful lever on EBITDA margin under declining revenue scenarios
- **Rationalize unprofitable products or SKUs.** The math you did a month ago may no longer be relevant; the list of products destroying value, consuming cash and other scarce resources, and adding supply chain complexity may now be much longer. Identify products with negative "operational contribution margin", assess their role in the product portfolio, kill or pause targeted products, and focus resources on the real margin drivers in the business
- **Adjust to new variability in demand**. Reduce unit production cost and control service levels through new production scheduling, and sales and operations communication routines
- **Reduce 3rd party supply costs** through supplier consolidation and renegotiation. There is a unique opportunity in the current market environment to do this
- **Proactively manage pricing and sales policies.** Avoid margin erosion through uncontrolled discounting, extension of payment terms, or timing of A/R
- **Refocus sales and marketing resources** to concentrate on the most relevant products, customers, and channels – follow shifting demand in the new market
- **Do the right-sizing work that has been deferred over time.** Scale down back office costs. Re-examine projected procurement, HR, IT, and finance/accounting transactional volume and staffing requirements

- **Shed or defer IT maintenance costs** while preserving your critical databases; rationalize software seats

4. **Continue frequent management of stakeholder communications throughout the restructuring process.** Employees, customers, key suppliers, and lenders are your most important assets and any one of these groups can derail your efforts

Many middle market companies have a difficult road ahead. It is not always obvious what to do and in what order to survive in the short term, prosper in the medium term, and thrive in the longer term. TriVista has specialized expertise and processes and can provide bandwidth to drive an immediate response. If you'd like our help, or simply want a sounding board to discuss options and strategies, please don't hesitate to reach out.

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About TriVista

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