

Leadership in the Distressed Organization

By Tommy M. Onich

Leadership is the most crucial factor in corporate recovery.

Distressed organizations face an environment that is harsh, unforgiving and ambiguous. Multiple and interrelated problems combine with numerous threats from multiple stakeholders. As time passes without action, things only get worse. At the same time, decision making is impaired by flawed or imperfect information. In this environment, leadership is crucial for recovery.

This article will examine the nature of effective leadership in the distressed organization. It will describe the characteristics that lenders should look for when evaluating the likelihood that existing management will be able to execute a turnaround by a distressed borrower.

Management and Leadership: Different and Complementary

Management and leadership are two distinct and complementary systems of action. Both management and leadership are necessary for success in the volatile and complex environment of the turnaround.

Not everyone can be good at both. Management is about coping with complexity. As large organizations evolved, management practices and procedures developed to bring order and consistency, for example, to ensure quality and profitability of products or compliance with safety regulations.

In contrast, leadership is about coping with change. It is not mysterious or mystical and has nothing to do with exotic personality traits or charisma. Having been involved in dozens of distressed organizations, I believe that charisma is the last thing employees want in a leader.

Leadership has become more important as the business world has become more competitive and volatile. Increased international competition, faster technological change, the deregulation of markets and unstable energy prices call for leadership.

In a custodial environment, the organization can carry on with good administration and management throughout its hierarchy, complemented by good leadership at the very top. In distress, the organization must have competent leadership at all levels.

Leaders Embrace Change

The 19th-century philosopher William James described two basic personality types: "once-born" and "twice-born." The once-born have had lives that were straightforward, following a peaceful flow since birth. The twice-born have faced many challenges in lives marked by constant struggle. James posits that these personalities have very different views of the world. These differences are relevant when we look at managers and leaders.

Managers see themselves as conservators and trustees of an existing order with which they personally identify. The self-worth of the managers is enhanced by strengthening and perpetuating these institutions, that is, by investing in the status quo.

Leaders tend to be twice-born personalities. They are not invested in the status quo and often seek opportunities for change. This is important because a leader is a catalyst for change as well as the architect and implementer of strategy.

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Leaders Think Unconventionally

We are drawn to stories of leaders in action. Their bold moves fascinate us. We seek to emulate their decisiveness. We are gripped by narratives of their successes and seek to analyze the elements of their character. We tend to believe that their actions are of great import. But the focus upon what a leader does is misplaced.

Examining strategic moves or execution in one context often makes little sense in another, sometimes even in the same organization. The organization in distress creates an environment that is ever-changing, replete with ambiguity, lacking resources, rich with threats and lacking in complete and accurate information. In this environment, emphasizing just what leaders do and the actions they take is fraught with peril. A more productive approach is to focus on how a leader thinks. Given the nature of corporate distress, examining a leader's cognitive process is far more important than examining a leader's past actions.

Conventional thinkers often face serious challenges in the distressed environment. They are disturbed by time and information constraints and unsettled by ambiguity and complexity. When they respond to challenges and problems, they:

- determine relevance by focusing on the obvious.
- tend to be linear.
- reduce problems and work on them sequentially or separately one at a time.
- quickly make choices that are either/or and settle for what appears to be the best option.

By contrast, the unconventional thinker will:

- examine relevance by also examining less obvious factors.
- consider more complex relationships among variables, including those that are multidirectional and nonlinear.
- see problems as part of a whole puzzle, examining how all of the pieces fit and how one decision can affect another.
- resolve ambiguity among ideas with creativity and synthesis seeking innovative outcomes.

The unconventional thinker fits the urgent environment of the distressed organization. In fact, many experienced chief restructuring officers (CROs) embrace such an environment and are suitable for little else.

Leaders Influence Others

In a distressed organization, resistance to change is often compounded by a nearly pathological denial in the face of evidence of corporate decline. Reluctance to change is exacerbated by the fact that organizational recovery will likely impair nearly all stakeholders. Some employees will lose their positions, creditors will not recover all of the money they are owed, suppliers will see a reduction in revenue, and pensioners may see a reduction in their benefits.

Therefore, the leader must be able to influence others. We call this ability "emotional intelligence," which has five components:

- **Sense of self.** People with a strong sense of self are honest with both themselves and others. Self-aware people tend to be confident while recognizing their limitations. They understand how their feelings affect them and others. They express themselves openly and with candor.
- **Discipline.** Discipline, or self-regulation, prevents us from being prisoners of our feelings. Leaders need discipline to create an environment of trust and fairness. This makes it easier to attract and retain talent.
- **Drive.** Leaders are driven to achieve beyond expectations. They display a passion for their work for its own sake. Their tenacity and energy serve as an example to others.
- **Empathy.** Empathy, the ability to identify with and understand another person's feelings, can seem out of place amid the tough realities of the marketplace. But empathy helps leaders understand the effect of change on others and find ways to solicit cooperation.
- **Social skill.** Leaders know that rapport and consensus are necessary for recovery. Social skill, while not manipulative, is friendliness with a purpose.

Assessing a Turnaround Leader

As an organization's environment changes, its leaders need to reevaluate whether or not its leadership can meet the challenges of the new environment. Simply put, are they a good fit?

Lenders can ask three questions to evaluate leaders of distressed businesses:

- **Does the leader have the honesty and integrity necessary to gain the support of all stakeholders?** Successful recovery will require the literal or figurative vote of all stakeholders, although their interests will be compromised. At least some stakeholders will need to provide continuing support. The leader must demonstrate honesty, integrity, transparency and high standards.
- **Has the leader demonstrated the ability to detach himself or herself from the status quo?** Can the leader quickly make difficult or even hurtful decisions? Recovery will require substantial, meaningful change, including the sacrifice of vested interests. The leader cannot be encumbered by emotion or prejudice.
- **Has the leader demonstrated an ability to cope in a deadline-driven, ambiguous environment with numerous threats and impaired information systems?** In the face of corporate decline, the environment is demanding in the extreme. Few individuals are suited to this environment; some actually embrace it. Fit is very important, and a lack of it will result in failure.

If answers to these questions raise doubts, existing leadership should be replaced or supplemented with an experienced CRO.

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