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This Year Not A Rerun Of 2010 For Corporate Restructuring Pros

By Kenneth R. Yager II

In 2011, the economy will continue to sputter and opportunities will abound for those in the turnaround industry, Turnaround Management Association members predicted in a recent survey that was the basis of a TMA webinar, "2011 Industry and Economic Forecast - We Are Not Out of This Yet" in January.

Asked whether the recession had reached its peak, TMA members answered similarly to the way they did in the 2010 forecast. Nearly one in five respondents said the worst of the economic crisis is yet to come, and an additional 19% said that while they expect improvement, it won't happen until 2012 or later. Only 10% said that the first half of 2011 will bring improvement.

Coming from any other industry, these results would signal fear or anxiety. Coming from the turnaround industry, they are marks of optimism. But it is false optimism.

Business in the turnaround industry is slowing down. The FDIC's September 2010 Quarterly Bank Call Reports showed that third-quarter commercial and industrial loan delinquency rates were down on both year-over-year and quarter-over-quarter bases. The recovery process is clearly underway and turnaround professionals need to adapt.

Looking at the breakdown of industries in which TMA members predicted signs of trouble, it's hard to see any justification for the notion that the economy is continuing to slide downhill.

Two key drivers of the recession were the automotive industry and the real estate industry. Yet only 7% of survey respondents expect the automotive industry to be one of the most troubled sectors in 2011, a sharp decrease from the proportion expecting automakers to struggle in 2010. Thirty-seven percent of respondents said they expect that the automotive industry actually will be one of the most improved industries in 2011. As far as Detroit is concerned then, the mechanic has come and gone and the "check engine" light is now off.

Regarding real estate, the other major driver of the recession, 64% of respondents said they expect commercial real estate to be among the most troubled industries in 2011. Forty percent put residential real estate near the top of the list, an increase from the forecast for 2010.

However, predictions of real estate troubles do not translate into a forecast of continued economic turmoil. The real estate market was severely shaken and most likely will remain vulnerable during the next few years, just as it did after the 1990 recession. But while the healing process will be slow, it has at least begun.

When respondents were asked to identify the top two external factors most likely to trigger problems for industries facing distress in 2011, they overwhelmingly selected "economic conditions" as the main culprit, apparently supporting the conclusion that more economic turbulence is ahead. But in the majority of industries about which respondents registered significant or growing concern, industry-specific problems are, in fact, the main source of potential difficulties.

For example, the main obstacle facing the real estate industry isn't the economic climate, but overcapacity. There is simply a glut of available properties. A similar problem exists in the retail industry, which 26% of respondents ranked among the top three most likely troubled industries. Despite the long-term trend toward online purchasing, brick-and-mortar retail space has increased over the past 10 years.

While not generating as much concern compared to other industries, transportation jumped significantly in ratings of distressed industries from the last annual forecast. Yet its problems are also deep-rooted and systemic, rather than the consequences of overall economic conditions. There is therefore little chance that it will replace the automotive industry as a driver, or indicator, of recession.

As the economic environment recedes in significance as a primary cause of distress, government policy and regulatory changes will play a substantial role. Regulatory changes rated as the second most important cause for concern after economic conditions and that points to uncertainty over the future of the extended Bush-era tax breaks and health-care reform as one of the biggest influences on the 2011 economy. Survey respondents were split on their predictions about the performance of the health-care industry in 2011. While 17% thought it would be one of the most troubled industries - a twofold increase from the 2010 forecast, 24% said it would be among those industries showing the most improvement in 2011.

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The economic crisis is on its way out, and on its way in is an era of normalcy during which the success or failure of specific industries will depend more on internal problems and specific government actions. The result will be leaner years for the turnaround industry, but that doesn't mean the coming years will not offer their own opportunities.

The majority of respondents - 35% - thought the bulk of cash reserves accumulated in 2010 would be spent on mergers and acquisitions. Academic studies have shown most acquisitions are not successful and that observation suggests M&A activity may produce a wealth of turnaround management opportunities. Companies involved in M&A often accumulate too much debt, a factor cited by 70% of respondents as one of the main internal causes of business distress.

Many turnaround professionals are still looking at 2011 as though it were a second 2010. It is time now to face reality and start pursuing the opportunities the New Year will actually bring.

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