

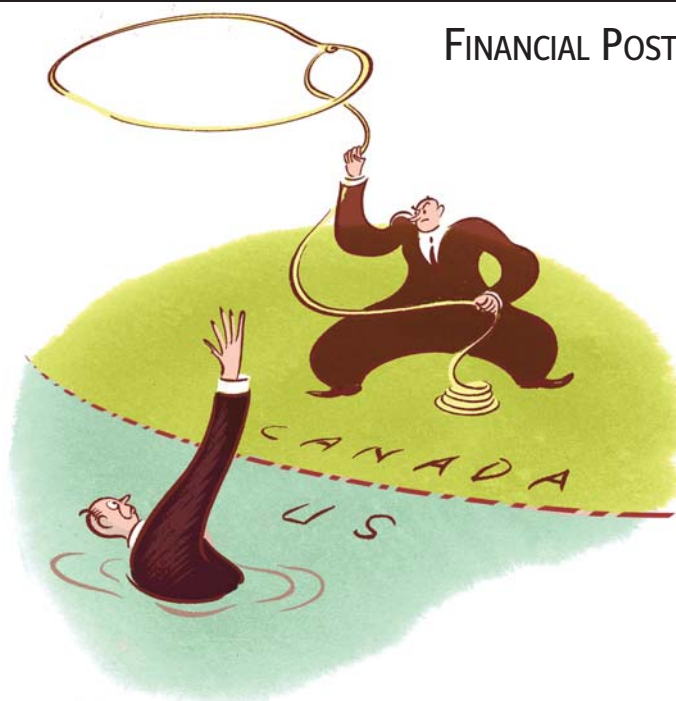
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Getting out of Trouble

Expansion and acquisitions help make a great business. But when those new ventures falter, leaders have to make things right. Or else



The company: Paradigm Foods Ltd. is the largest family-owned food distribution business in Canada. Founded by Tom Graham, a food-service industry sales veteran, it distributes bottled soft drinks, water, chocolate and other foods to hotel and grocery chains nationwide. Its subsidiary, Paradigm Foods Inc., does similar work in the U.S.

The situation: Paradigm's Canadian operations are flourishing. But the same can't be said for its U.S. subsidiary. After 13 years in business and one recent major acquisition, it has yet to turn a profit. Graham and his U.S. president, Larry Prado, have spent too many hours on the problem. His patience spent, Graham has ordered Prado to develop and implement a plan that will make the business profitable within the next year.

IT WAS A BALMY, midsummer's evening in Montreal. Tom Graham was sitting in just about the last place he really wanted to be: behind his office desk, punching numbers into the telephone. Graham, president and owner of Paradigm Foods Ltd. (PFL), Canada's largest family-owned food distribution company, had spent the past couple of hours studying the latest quarterly results from its U.S. subsidiary, Paradigm Foods Inc. (PFI), and he was less than pleased with what he saw. Heading into the company's fiscal fourth quarter, Paradigm's U.S. operations were on the verge of losing money for the third year in a row.

Graham leaned back in his chair as the phone rang at PFI's head office in Pasadena, Calif. Larry Prado, the U.S. subsidiary's president, picked up the line. He'd been expecting the call – the two men talked regularly and PFI's struggles were hard-

ly new. What's more, they had a long history together – Graham hired Prado to be PFI's president in 1990, when he established the subsidiary, and they'd been working together ever since.

After some quick pleasantries, Graham got to his point. Several weeks earlier, he had sent Prado a lengthy note outlining some key questions about PFI's business that he felt Prado needed to address.



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ILLUSTRATION BY ERIC PALMA

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Now he wanted Prado to pull together his management team to tackle these questions and come up with a fresh, coherent strategy. To underscore his request, he made it clear to Prado that he expected PFI's operations to be profitable within the next 12 months – and that he expected the subsidiary to double its revenue over the next five years without a major infusion of capital from its Canadian parent. Given the time horizons involved, it wasn't exactly an ultimatum. But it came close.

Prado put down the phone, wondering how he could meet the challenge. In Canada, over the past eight years, Paradigm had more than tripled its revenues and grown profitability by an even larger amount. It was now a leading distributor of bottled soft drinks, water, chocolate, biscuits and crackers, cheese, and preserved fruits and vegetables. Its larger customers included hotel chains, grocery chains and some smaller distributors. But in the U.S. – where the business operated chiefly in two regional markets, the northeastern seaboard and the west coast – it had been year after year of stagnation. Despite making a significant acquisition in 2000 that doubled revenue to US\$75 million and added a number of talented people to the organization, PFI's bottom line had remained unchanged.

Making matters worse, it was obvious there would be no simple fix. In the West, fierce competition was a problem, costing PFI money and customers. While the business on the east coast, which PFI acquired in the 2000 purchase, was at least in the black, that was largely due to the efforts of a handful of talented, if somewhat cavalier, salespeople. That side of the organization was poorly organized and had not adapted well to the change in ownership. Between east and west, meanwhile, PFI did not have the same makeup in terms of its product portfolio and customer

base. If Prado knew anything for sure, it was that he had an awful lot on his plate.

TO GRAHAM, AT LEAST, the best place for Prado and PFI to start would be in reviewing Paradigm's own history in Canada. Graham, who'd worked nearly two decades in food industry sales, created PFI in 1985. The opportunity arose when Fichelle Ltée, a French beverage company, decided it wanted to find a distributor for its products in Canada. It was Fichelle's decision in 1990 to expand sales into the U.S. that prompted Graham to create its U.S. subsidiary, PFI, and hire Prado to run it.

However, it was the next major event in Paradigm's history that Graham now felt held the key for PFI's troubles in the U.S. – specifically, its 1993 acquisition of Robinson & Fitch, a small regional player on Canada's west coast. Taking it over solidified PFI's national position, but left it with two separate operating organizations and two distinct cultures – the same situation now playing out in the U.S.

The fix in Canada took years. Things first got rolling in mid-1995, when Graham decided PFI had two related problems – it was neither sufficiently focussed nor differentiated from its competitors. To tackle this problem, he organized a pair of workshops in which his entire management team took on these issues.

In the first workshop, the team assessed PFI's strategic performance. Their analysis revealed that the company had too many underperforming suppliers and customers. So much so, that one-quarter of its customers accounted for almost three-quarters of profits, while just five suppliers, out of 64 in total, represented 65% of revenues and 80% of profits.

In the second workshop, management developed a strategy that they felt was unique in food distribution in Canada. At its heart was a business model that Graham characterized as

supplier- and customer-centric. In future, Paradigm would focus its sales efforts around a relatively small set of products from a group of core suppliers that it would use to secure new accounts. Once established, though, Paradigm would seek to fulfill as much of its customers' food product needs as it could, from a wider array of suppliers. However, this meant that over the next few years, Paradigm would deliberately drop many of its less profitable suppliers and a number of existing customers.

For the next couple of years, PFI showed little improvement. That's when Graham decided to make some sweeping personnel changes. The reason: He realized that some members of the existing sales force were unable to stop selling to unprofitable accounts and, more importantly, unwilling to increase the time they spent prospecting for new business. Over the next year, seven out of 18 sales representatives were replaced by individuals aligned with the new sales strategy.

Graham also moved out a couple of members of his senior management team and, by late 1997, "everything clicked into place." In 1998, Paradigm's sales started to grow. While profitability, at first, remained low, company morale soared. Over the next two years, both sales and profitability grew faster than at any time in Paradigm's history. In 2000, the strategy exercise was repeated, and a new vision – "Vision 2005" – was established for Canada. By the end of 2002, it was clear to Graham that the Canadian company was performing extremely well and on target. Accordingly, his attention now turned to the U.S. subsidiary.

SINCE ITS FOUNDING, PFI had never had a profitable year of operations. Initially, Fichelle had targeted California for its U.S. expansion, and that had been the target for PFI as well. But while Fichelle's sales grew rapidly, PFI had

INNOVATIVE IDEAS.
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a hard time securing exclusive distributorships in the market with other food product companies. A number of international firms that Paradigm represented in Canada already had distribution in the United States. Meanwhile, U.S. manufacturers typically either distributed themselves, or had established relationships with domestic distributors. Accordingly, while PFI was able to secure a number of exclusive distributorships with lesser known European producers, over 50% of its sales came from non-exclusive products. Margins on these were typically smaller than on its other products.

company officials assured Graham and Prado that they would continue to have distribution rights for Fichelle products in the U.S.

That's when Prado proposed to Graham that PFI acquire Great Eastern Products, a failing distributorship based in Newark, N.J. Its customers were primarily in the northeast but it had representation up and down the eastern seaboard. Great Eastern had been very profitable a few years earlier, but a split in its management ranks had resulted in a number of its key executives and sales staff departing, and taking with them many of the firm's most prof-

Despite this imbalance, it was clear to both Prado and Graham that any solution for PFI needed to be integrated across the entire subsidiary. In their conversations together, Prado had stressed how totally different the eastern business was from that in the West. The product mix was different, suppliers were different and the entire culture of the eastern business was different. In the East, Paradigm had acquired a business with many small accounts and a wide assortment of non-exclusive products. Sales were made on a highly opportunistic basis, and the sales force acted almost as

In their conversations, Prado stressed to Graham how totally different the eastern business was from that in the West. The product mix, suppliers, even the culture in the eastern business was different

Similarly, it proved difficult for PFI to secure business with national chains. Being a regional distributor, PFI was largely limited to doing business with small and medium-sized local businesses. While some of these accounts were profitable, there was tough competition from other regional distributors for this business. Even when PFI expanded its operations to cover the entire west coast, it still could not attract larger companies.

Fichelle's management, meanwhile, was growing impatient. It wanted to attack the entire U.S. market, and in 2000 announced that it would not only be setting up a plant in the U.S., but that it would also begin recruiting its own sales force. However, because of their excellent relationship with Paradigm in Canada,

itable customers. However, in Prado's opinion, Great Eastern still had some viable accounts, an excellent logistics infrastructure and a number of talented, if young, sales employees.

The deal closed late in 2000. Both Prado and Graham spent a considerable amount of time in Newark for the first year, familiarizing themselves with the business and getting to know the employees and key customers. Fichelle was rapidly incorporated into the product line of the new business, and sales grew rapidly. Surprisingly, profitability came easily to the new acquisition, and the new operations boosted the U.S. bottom line in both 2001 and 2002. However, continuing problems in the western operations were still a drain on overall results.

independent agents – some very successfully, others less so. For example, the top three salespeople virtually refused to file sales plans or activity reports, and knowing how dependent Paradigm was on their efforts, they had little fear of consequences. Moreover, they simply ignored Prado's suggestions to drop low-profit accounts and focus on those with higher potential. As Prado commented: "They just do what they want, and they know in our current position it's hard for me to discipline them."

IT WAS IN THIS CONTEXT, and in the face of continued poor performance in fiscal 2003, that Graham sent Prado his recent notes and pushed him to set up a strategy workshop with his senior staff. In the letter, he reminded

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Prado of Paradigm's experiences in Canada. He also outlined a number of key questions and potential strategies that had to be discussed.

The questions Graham raised were familiar to Prado. First, was the PFI business model appropriate to the U.S. environment and marketplace, or would a different model have to be developed? If so, what model would deliver the level of growth and profitability that Graham was expecting? Second, and of equal importance, should PFI become a national company or remain a regional player? Third, with the continuing emergence of domestic specialty food companies and the ongoing rise of the Euro against the U.S. dollar, was the European sourcing strategy going to be viable in the United States?

Prado was also concerned about both regional operating groups, but for different reasons. In the West, achieving profitability seemed like an elusive dream. In the East, the whole issue was focus. Both Prado and Graham could see dramatic improvements in profitability, if only they could get their sales force to focus on profitable accounts and product lines. A key issue here, Graham believed, was that the company needed to hire a senior second-in-command to Prado, who would be based in Newark full-time.

Prado felt that he and Graham worked well together, and he valued Graham's advice to focus on a few things and do them well. However, he also knew that Graham had dictated such an approach when he said he wouldn't put any more money into the firm. Prado looked upon the upcoming strategy sessions with a mixture of hope and trepidation. What would the future strategy look like? And what process was required to develop a strategy capable of meeting both his expectations – and Graham's – over the next five years?

The Outcome

PRADO HELD TWO strategic planning sessions for PFI involving all the key players from the U.S. In the first session, the group had a complete, honest discussion about the U.S. situation, identifying key challenges and a number of opportunities for revenue and profit improvement. In the second session, held a month later, the group developed a five-year vision for the company, and more importantly

a 12- to 18-month turnaround "mission" with clear objectives for both the northeast and the west coast. The plans included strategies to improve territory sales effectiveness, elimination of unprofitable customers and suppliers in each region, changes in product mix to improve profit margins, a game plan to secure the Fichelle account, and agreement on a revised compensation plan for the sales force.

Prado resisted any proposal to hire a strong second-in-command for the U.S. to run the northeast. But because family commitments limited Prado's ability to travel, that meant Graham had to commute regularly from Canada to work with the eastern group. Sales and profit performance were closely monitored, and the strategy for the U.S. was reviewed and updated every 100 days. Sales force staff were replaced as it became clear that certain individuals could not – or would not – align themselves with the strategy.

Positive results were achieved very quickly. PFI was profitable within six months, and after-tax profits exceeded \$1 million in fiscal 2003, and over \$3 million in 2004. Morale soared. However, Prado remained unwilling to spend much time in the northeast, and Graham continued his commutes from Canada.

In late 2004, the owners of a fast-growing U.S. food distributor approached Graham, asking if he was interested in selling the U.S. operations. Six months of negotiations ensued, at the end of which Graham sold PFI Inc. for a sum in excess of US\$30 million.

The Expert View

By Peter Richardson

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IN THIS CASE, the solution to the business problems was very straightforward. The strategy that was developed by the team in the U.S. was basic "blocking and tackling." Decisions on suppliers, products and people that had needed to be taken for some time were finally taken. More compelling and instructive, however, is the way Tom Graham's frustration with Larry Prado's leadership style grew – and how Graham did, or did not, deal with it.

Clearly, Graham possessed a superior understanding of the food-distribution business, in which he had spent his entire career. He built a business in Canada that was inherently entrepreneurial, but based on a well-developed sense of strategy and a strong sense of teamwork among the management group.

Prado, in contrast, was primarily tactical and never took the initiative to develop a sound strategic plan for his subsidiary. In addition, nearly three years after the eastern acquisition, he had not created a strong sense of teamwork in PFI. In fact, the culture of the U.S. subsidiary was fractious and unaligned. Also, Prado was unwilling to spend time in the East, where leadership was sorely required.

But while Graham was unhappy with Prado's leadership, neither was he willing to replace him. Consequently, Graham had to step in personally and lead the turnaround. Graham kept hoping that Prado would get the message about his leadership style, but in fact, Prado seemed content to ride on the success that Graham's intervention had created.

Even if Graham knew that Prado was not the right person to lead the U.S. subsidiary, a strong sense of personal loyalty kept him from replacing him. But Graham also wanted to spend less time running the business. And so, in 2005, he appointed a new Canadian president. When he was quickly accepted, it highlighted Prado's deficiencies even more. Consequently, when it became clear that Graham would have to continue supporting the U.S. operations indefinitely, the offer to sell at a good price, when it came, proved irresistible.

Note: The authors do not intend to illustrate either effective or ineffective handling of a managerial situation. The views represented here are solely those of the case authors and are based on their own professional judgment. Company names, scenarios or identifying information may have been disguised to protect confidentiality.