4. THE FRAMEWORK FOR ACHIEVING A SUCCESSFUL TURNAROUND

A successful turnaround depends upon developing an appropriate turnaround prescription and effective implementation. The first point addresses "what" needs to be done and the second point "how" to do it. We have developed an approach for achieving a successful turnaround which consists of seven essential ingredients and an implementation framework consisting of seven key workstreams. This chapter outlines the framework, and subsequent chapters develop the approach in further detail.

SEVEN ESSENTIAL INGREDIENTS

Recovery of a sick company depends upon the implementation of an appropriate rescue plan or turnaround prescription. Characteristics of the appropriate remedy are that it must:

- address the fundamental problems;
- tackle the underlying causes (rather than the symptoms);
- be broad and deep enough in scope to resolve all of the key issues.

One of the challenges for any turnaround leader is to ensure that the rescue is built on a robust plan. Plans that try to tackle every single problem of a troubled company, no matter how big or small, will fail as limited resources are wasted on tackling 'non mission critical' issues. The key is to focus on tackling the life threatening problems. A recovery strategy that is based on the symptoms rather than the underlying causes may make the patient feel better temporarily but any long term recovery strategy has to be based on sorting out the underlying causes of distress. Turnaround plans must be sufficiently broad and deep to ensure that all of the mission critical issues are addressed. Turnaround management involves radical rather than incremental change. Very sick companies have serious problems which can only be tackled through fundamental, holistic recovery plans. In our experience, we have almost never encountered a turnaround plan which was too drastic. The chief danger to avoid is doing; "too little too late".
A successful turnaround or recovery plan consists of seven essential ingredients:

1. crisis stabilisation;
2. leadership;
3. stakeholder management;
4. strategic focus;
5. organisational change;
6. critical process improvements;
7. financial restructuring;

Successful turnaround situations are characterised by significant actions in each of the seven areas. Failure to address any one of these may endanger the successful outcome of the turnaround.

We put crisis stabilisation at the top of our list because it plays a critical role in any successful recovery situation. By securing a short term future for the business the turnaround leader creates a window of opportunity within which he or she can develop and implement medium and long term survival plans. Creating that short term breathing space is an essential prerequisite for a successful turnaround, as is our second ingredient, strong leadership. Our final ingredient addresses the prerequisite of establishing a sound financial base and appropriate funding for the recovery.

The third ingredient addresses the critical role of stakeholders in the recovery process and the importance of both reconciling their often conflicting needs and rebuilding their confidence.

The next three elements recognise the integrative nature of a business. Successful organisations are based on developing a viable strategy, and then aligning and integrating it with an appropriate organisational structure and effective business processes.

Each of these core areas of the turnaround plan is supported by a range of generic strategies which address the problems most usually encountered under each of the
seven areas. Our list of generic strategies is set out in figure 4.1. Clearly it is not an exhaustive list since each situation has its own specific characteristics that require a tailored solution. Nevertheless, there are a number of actions that are sufficiently common to most situations that we consider them to be generic turnaround strategies. There are discussed in detail in the chapters that follow, but first we must give the reader an overview of each of the seven ingredients.

(1) Crisis Stabilisation

In most turnaround situations crisis management will have to commence immediately. Substantially underperforming companies typically suffer from a rapidly worsening cash position and a lack of management control. In many situations companies are in ‘free fall’; senior management are paralysed in the face of an apparently hopeless situation and the business faces the very real prospect of running out of cash in the very short term. The turnaround manager or whoever has effective management control at the time must move very rapidly to take control of the situation and commence aggressive cash management.

The objectives of crisis stabilisation are:

• to conserve cash in the short term and thereby provide a window of opportunity within which to develop a turnaround plan and agree a financial restructuring;

• to rebuild stakeholder confidence by demonstrating that senior management have taken control of the situation.

The approach requires very strong top down control. The turnaround manager moves quickly to impose a very tight set of controls for the entire organisation. Devolved authority to spend money, incur credit, commit the business etc is removed. Short term cash generation becomes the top priority.

A critical element is to rebuild predictability into the business and the generation of rolling short term cashflow forecasts become a key management tool. The process of forecasting the short term cash position, communicating the information to the stakeholders on a regular basis, and then subsequently achieving the forecasts is crucial in rebuilding their confidence. Crisis management requires very robust
leadership; in most cases the turnaround manager is forcing a radical mindset change on the organisation.

The other key element is launching a series of cash generation strategies. Working capital is reduced by liquidating surplus stock, improving debtor collection and stretching creditor payments. All capital expenditure, except the most essential is put on hold. Sometimes there is an opportunity to increase short term revenues by price increases or provisional events – but this is the exception rather than the rule.

<table>
<thead>
<tr>
<th>Seven Key Ingredients</th>
<th>Generic Turnaround Strategies</th>
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<tr>
<td>1. Crisis Stabilisation</td>
<td>• Taking control&lt;br&gt; • Cash management&lt;br&gt; • Asset reduction&lt;br&gt; • Short term financing&lt;br&gt; • First step cost reduction</td>
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<tr>
<td>2. Leadership</td>
<td>• Change of CEO&lt;br&gt; • Change of other senior management</td>
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<td>3. Stakeholder Focus</td>
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<td>4. Strategic Direction</td>
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<td>5. Organisational Change</td>
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<td>6. Critical Process Improvements</td>
<td>• Improved sales and marketing&lt;br&gt; • Cost reduction&lt;br&gt; • Quality improvements&lt;br&gt; • Improved responsiveness&lt;br&gt; • Improved information and control systems</td>
</tr>
<tr>
<td>7. Financial Restructuring</td>
<td>• Refinancing&lt;br&gt; • Asset Reduction</td>
</tr>
</tbody>
</table>

Figure 4.1 Generic Turnaround Strategies

(2) Leadership
New Chief Executive

Inadequate senior management is frequently cited as the single most important cause of corporate decline, and therefore many, but not all, turnaround situations require a new Chief Executive Officer (CEO). Many investors and turnaround practitioners argue that in almost every case a change of CEO is required for two reasons. The first point is that since the CEO was the principal architect of the failure it is very unlikely that he can form part of the solution. The second argument is that a change of CEO has enormous symbolic importance; it sends a strong message to all stakeholders that something positive is being done to improve the firm’s performance.

An alternative view is that the immediate removal of a CEO may not be in the best interests of the company. It is a decision that may make stakeholders feel positive in the short term but which they may come to regret at their leisure. It is important to remember that many CEO’s of troubled companies have a strong track record of prior success; today’s villain was yesterday’s hero. Furthermore, the CEO is often the person with the most knowledge and experience of the company and the industry; skills that may be vital to the recovery.

A second important consideration is the type of CEO to appoint to a turnaround situation. The basic choice is between a candidate with substantial industry expertise but no prior turnaround experience or the converse, an experienced turnaround manager or company doctor. The appropriate choice will inevitably depend on the specific circumstances. On balance, however, we would tend to favour a candidate with previous turnaround experience rather than industry knowledge for most situations. A good company doctor is usually a highly effective general manager, and experience suggests that effective general managers can usually work across most industries, other than the most specialised.

A further consideration is whether one person can lead an organisation through the complete recovery process from crisis stabilisation to restructuring and on to corporate renewal. The manager who is good at taking control, generating cash, downsizing and cutting costs is often no good at developing and implementing viable market-lead strategies for the longer term.
The immediate task of the turnaround leader is to rebuild stakeholder confidence by re-establishing a sense of direction and purpose. The leader must move quickly to initiate the development of a rescue plan, and communicate it to stakeholders. Finally, the leadership must be seen to be taking action quickly; it is essential to achieve some “early wins”.

Other Senior Management Changes

Apart from the change of CEO, many turnaround situations are characterised by other senior management changes. Again views vary enormously among experienced company doctors. There are those who argue for wholesale change, irrespective of the competence and willingness to change of the incumbent management. Proponents argue that such action eliminates resistance to change, sends a strong message throughout the organisation, and is a necessary part of the shock therapy that troubled companies require. The opposing view is that, as far as possible, the new CEO should work with existing management, with the proviso that the individuals are sufficiently competent and show a willingness to change. Irrespective of which approach is taken, most turnaround managers will introduce a new finance director because of the critical importance of strong financial management in a turnaround environment.

Turnaround managers rarely have the luxury of working with a world class management team and workforce. However, large scale management change is rarely an option in the early days because it is not easy to attract good managers to highly unstable situations. Consequently, one of the major leadership challenges for the turnaround manager is to deliver superior performance from a relatively weak team.

Notwithstanding the above point the organisation requires sufficient human resource for the challenge ahead. Embarking on a turnaround with a team that lacks the basic expertise and experience required is a foolhardy exercise. At the early stage the turnaround leader needs to conduct a rapid management skills audit. The objective is to establish where the “gaping holes” exist and to consider ways of filling the skill gaps. At the very least most organisations require effective financial, operations and sales and marketing management.
Improved Communications

Most companies could have better internal communications, but in a turnaround situation a quantum leap is usually necessary. As the company has gone into decline less and less information has been communicated, cynicism has increased and morale has declined. The turnaround manager and his top team have to develop external credibility very quickly if they are to harness the organisation’s resources. They therefore have to decide what to communicate, how to communicate it, to whom and where. In doing this it is crucial that they all communicate the same message.

Building Commitment

An early stage initiative for the turnaround leader is to motivate the whole workforce. His priority here is to prevent good people leaving and to start to mobilise the organisation for the challenge ahead. Particularly during the early stage of the recovery, the organisation will move through a very turbulent times and having a committed workforce is a key factor for success.

(3) Strategic Focus

Substantially under performing companies generally face one or more serious strategic problems. Strategic issues are invariably “mission critical” because they impact the raison d’être of the business. Few organisations have a natural right to exist. Continued existence depends upon establishing a business that delivers a service or product in such a way that it generates a return on capital that exceeds its cost of capital. This requires a robust and viable strategy that incorporates a clear sense of purpose and direction, realistic long term goals that are based on genuine commercial opportunity, viable plans for achieving those long term goals and an ability to outperform competitors based on genuine competitive advantage. Our experience with troubled companies is that they very rarely have a robust and viable strategy. Typically, a formal strategy has not been clearly articulated and written down resulting in confusion across the organisation. Any strategy that exists is usually based on long term goals that are either unrealistic or lack commercial common sense. Alternatively the business may not be well equipped to achieve its long term goals lacking the basic resources and capabilities required to develop any competitive advantage.
The key business objectives for a turnaround manager is to develop a recovery plan that tackles these generic problems.

All the basic principles of strategic planning apply in turnaround situations. The strategic problems faced by most troubled companies, although very serious, are rarely complex. The solutions tend to be simple in concept but more complex in their execution. The desired end state or vision for the business must be clearly understood across the organisation. That destination must be intrinsically attractive, ie profitable and based on an underlying demand for that service or product. The business must be capable of delivering a range of services or products, taking into consideration the resources it has at its disposal (infrastructure, people, know-how, technology etc) and it must be able to do so more effectively and efficiently than its competitors. The strategy must be written down and widely communicated throughout the organisation. It should incorporate a simple definition of the goals and objectives of the business. It should encompass the “what” and the “how”, ie what products/services are we going to deliver and to whom, and how are we going to do it.

The choice of strategy must take into account the existing resources and capabilities of the organisation. To the extend that the recovery strategy depends upon skills and capabilities that the organisation lacks, the gap must be manageable. A focus on the key success factors for the strategy must be a: the heart of the recovery plan, since they provide the parameters within which the entire recovery plan must be developed. The product/market mix provides the target or focus for the entire organisation; it defines what products/services will be sold to whom. The importance of clarity on this issue cannot be overstated. Establishing a viable product/market strategy must be based on identifying a genuine customer need.

In many cases the strategic analysis will have to be quick and dirty. In our experience it is better to be “80% right and act” than “100% right and have missed the opportunity”. Despite being “quick and dirty” the approach must be bold and broad. The danger for any turnaround leader is to use the excuse of insufficient time and analysis to postpone major strategic change. However a sense of balance is also required.
Below we set out a brief summary of the most common generic strategies used in recovery situations.

Redefine the Business

This is the most fundamental form of strategic change. The long term goals and objectives of the organisation are changed; the management mindset changes and the nature of the business is redefined. For example diversified multi industry conglomerates become industry specific focused businesses, vertically integrated companies split, and multi process organisations restructure around a single core process.

Divestment

A divestment strategy is often an integral part of product – market refocusing. As the firm cuts out product lines, customers or whole areas of business, assets are liquidated or divested. The focus here is the disposal of significant parts of the business (division or operating subsidiaries), rather than the liquidation of current assets or disposal of surplus plant and machinery which we consider to be part of crisis management.

Growth via Acquisition

A somewhat surprising but quite common recovery strategy is growth via acquisition. This does not necessarily mean diversification into new product-market areas totally unrelated or only marginally related to the firm’s existing business. It may mean the acquisition of firms in the same or related industries. Acquisitions are most commonly used to turn around stagnant firms: firms not in a financial crisis but whose financial performance is poor. The objective of growing by acquisition rather than by organic growth is related to the faster speed at which turnaround can be achieved by following the acquisition route. It is a strategy available to few firms in a crisis situation because they lack the financial resources to make an acquisition although, once survival is assured, acquisition may be part of the strategy to achieve sustainable recovery.

Product Market Refocusing

Less radical than a complete redefinition of the business but still involving fundamental strategic change is a refocusing of the product/market mix. This occurs
at the operating company or business unit level and involves the firm deciding what mix of products or services it should be selling to what customer segments. As we saw in Chapter 2 the distressed firm has usually lost focus by adding products and adding customers while continuing to compete in all its historical product or market segments. Pareto (80:20) analysis quickly shows that there is usually an excessively broad product range and broad customer base, much of which consists of loss-making or low margin business. In the early stage of turnaround the appropriate product market strategy usually involves exiting unprofitable products and customers and refocusing on those which are relatively more profitable.

**Outsource Processes**

Outsourcing addresses the position of an organisation within the value chain of the enterprise system within which it operates. The rationale behind outsourcing is to focus on profitable processes where the company has a relative advantage and to outsource the remainder to third parties who can perform them more effectively. Outsourcing one or more businesses or functions is a core element of enterprise transformation. Traditionally outsourcing has been applied to non-core support processes with a heavy emphasis on finance and information systems. Increasingly, however, it is being applied to core functions and processes as multi-process organisations restructure to focus on only one or two core processes. Outsourcing is equally relevant to turnaround situations and is one of the generic strategies available as part of a strategic change plan. The emphasis within a turnaround environment is usually the urgent need to replace or enhance a substantially ineffective process.

**Stakeholder Management**

Troubled companies typically suffer from poor relations with their key stakeholders. Stakeholders, comprising debt and equity providers, suppliers, customers, management and staff regulators etc can normally be split between “mission critical” and less important. The power, influence, and importance of stakeholders will vary according to each situation. In most cases some or all of the stakeholders will be aware of the distressed nature of the organisation and will be concerned primarily about their own risk exposure to a failure of the business. A history of poor trading, inadequate communications, unfulfilled promises from management, and unpleasant surprises, coupled with the risk of failure will have eroded their confidence in the business. The
other key issue is that the stakeholders will have different objectives and priorities. If the company is going to be rescued these differing agendas have to be reconciled and stakeholder confidence rebuilt.

The guiding principle is that the turnaround manager must start to rebuild stakeholder confidence through a process of open communications and the provision of reliable information. Predictability must be restored and unpleasant surprises avoided at all costs. The role requires both impartiality as regards facts but also a robust advocacy of the company’s position. Success depends upon getting the stakeholders to recognise and accept the reality of the company’s position and work co-operatively towards a solution to the business’ actual problems.

Gaining stakeholder support requires careful stakeholder management. The first stage involves the clear unbiased communication of the company’s true financial position to relevant stakeholders. Based on that the turnaround manager can commence a preliminary assessment of stakeholder positions, and identify at an early stage the level of support a for turnaround plan (compared to other options such as sale, insolvency etc). It may be necessary to reach a standstill agreement and negotiate ongoing support from the company’s bankers during this period. During the early stages of the turnaround, there should be regular communication of the short term cash and trading position. The turnaround manager should seek the involvement of stakeholders in the development of turnaround plans. Finally, the stakeholder’s formal approval and agreement to the company’s detailed rescue plan should be obtained. Ongoing communication of the trading performance and progress of the recovery should occur during the implementation process.

(4) Organisational Change

People problems are usually among the most visible signs of a troubled company. Typical symptoms include a confused organisation structure, a paralysed middle management, resistance to change and demoralised staff. Staff turnover is probably high, the most able people have left and the remaining workforce lack key skills and capabilities. Dysfunctional behaviour where employees fail to co-operate towards achieving the corporate objectives may be encouraged by silo thinking and a rewards system not aligned with the strategy. Significant organisational change is therefore required.
New Organisational Structure

Changing the organisational structure can be a powerful way of rapidly changing the operations of an ailing business. A revised structure that facilitates clear accountability and responsibility will make the implementation process more straightforward. The turnaround leader will be able to see clearly who in the organisation is delivering against the plan and who is not. Any revised organisational structure should emphasise an external market facing perspective, empower middle management and seek to breakdown “silo thinking”. As we shall see however in Chapter 10, structural change should be kept to a minimum in the early days of a turnaround.

The People

People are more important than structures. Capable and motivated staff are critical to an effective turnaround since it is they who have to implement whatever recovery plan is agreed. Thus a top priority task is assessing the people in the organisation - particularly the management - and deciding who, if anybody, should be changed and when. In undertaking this assessment it is as important to assess skills and capabilities as it is to assess attitude to change. One without the other is no good.

Building Capabilities

The generic strategies covered under process improvements all involve the organisation “doing things differently”. Activities and sub processes are reconfigured, organisational structures change, and new measures of success are introduced with the consequence that employees will have to be trained to work the new ways. Adequate training to support the change programme is therefore a vital element of successful recovery.

Terms and Conditions of Employment

We believe that an effective reward system can play a major role in tackling the people problems of a business. The entire organisation should be strongly incentivised to implement the recovery plan. It seems to us quite obvious that people who feel they have a stake in the business and who are financially motivated to implement a
recovery plan successfully are more likely to give their best efforts than those who are not.

In recent years changing contracts of employment and UMON agreements have also been used as effective mechanisms of organisational change.

(6) Critical Process Improvements

Substantially underperforming companies typically have serious problems with both their core and support processes. Processes are often characterised by high cost, poor quality and lack of flexibility/responsiveness. The underlying causes of these problems vary. Many processes are poorly managed due to a lack of focus on cost, quality and time. Problems with the physical infrastructure such as state of machine repair, outdated IT systems and an organisational structure that breaks natural links in processes can exacerbate problems.

The tools and techniques of mainstream business process re-engineering (BPR) substantially apply. However, it is important that the turnaround plan does not become a BPR project. Turnaround plans are broader and deeper than conventional BPR, even as originally conceived by Hammer and Champsy. The emphasis in turnaround situations is on “quick win” process re-engineering. Standalone BPR projects are typically characterised by a strong link with technology and management information systems (MIS) improvements. These projects tend to be large scale and long term with the emphasis on process improvements through improved computer technology. In a turnaround environment the reverse tends to be true. The approach is “quick and dirty” with the objective of focussing attention on the core processes. Typically this will cover procurement, conversion, logistics and sales and marketing. The emphasis is on achieving a rapid quantum leap improvement in time, cost or quality without the need for major MIS improvements.

Business process improvements generally fall within the following dimensions:

- Time improvements: typically the focus is to make the organisation more responsive and more flexible by reducing the time taken to bring a product to market or reducing manufacturing lead times.
• Cost improvements: the approach is to simplify processes to reduce both the fixed and variable costs.

• Quality improvements: this is self explanatory and is about reducing rework loops, systematically analysing the reasons for non conformance and putting in place corrective actions to improve processes.

Generic strategies deployed across the various business processes can be summarised as improvements to demand generation processes, demand fulfilment processes and support processes.

Demand Generation

Assuming that product-market refocusing decisions have been taken, improving the selling process and the effectiveness of the sales force is a key area for process quick wins. Marketing mix improvements include brand management/repositioning, promotions and particularly, pricing. New product development and improved customer responsiveness may also provide important improvement opportunities. Although this area tends to be more important in enterprise transformation rather than turnaround situations, increasing innovation rate and improved product engineering are important longer term initiatives.

Demand Fulfilment

Typically this is the core area for process improvements and will involve substantial cost reduction and improved effectiveness in procurement, manufacturing/conversion, logistics and after sales service. Simple procurement initiatives can reduce cost, working capital and inventory risk and improve quality and service. Gaining control of the shopfloor and improving efficiency typically involves layout changes and introduction of cellular manufacturing, JIT and Kanban principles.

Support Systems

The introduction of a production planning function to balance the supply and demand side of a business is an important generic response to a very common business problem. Other improvements will be targeted at “head office functions” and will include introduction of new performance measures, improvements to the management
of the physical infrastructure, and the restructuring of the finance department to deliver timely, relevant and accurate information.

(7) Financial Restructuring

Companies in need of a turnaround typically suffer from one or more of the following:

- Cashflow problems ie insufficient future funding or an inability to pay debts as and when they fall due.
- Excessive gearing (too much debt/too little equity)
- Inappropriate debt structure eg excessive short term/on demand borrowing and insufficient long term debt
- Balance sheet insolvency

Irrespective of the health of the underlying business, if the operating cash flow cannot finance the debt and equity obligations, the company will remain fatally wounded. In these circumstances the only solution is a financial restructuring.

The objectives of any financial restructuring are to restore the business to solvency on both cash flow and balance sheet basis, to align the capital structure with the level of projected operating cash flow, and to ensure that sufficient financing in the form of existing and new money is available to finance the implementation of the turnaround plan.

A financial restructuring usually involves changing the existing capital structure and/or raising of additional finance. Capital restructuring usually involves an agreement between the ailing firm and its creditors, usually the banks, to reschedule and sometimes convert interest and principal payments into other negotiable financial instruments. The raising of new funding may involve additional debt, typically from the existing lenders who may be persuaded that the best prospect of recovering their existing lending is via the provision of further lending. The provision of new equity from existing shareholders via a rights issue or from outside investors (vulture funds etc) frequently accompanies new bank lending.

THE IMPLEMENTATION FRAMEWORK
The starting point for the implementation of the turnaround process is always a diagnostic review to establish the true position of the troubled company and to determine whether a turnaround is a viable option, as opposed to insolvency, immediate sale or liquidation.

Once the decision to proceed with a turnaround has been taken by the principal stakeholders, seven separate implementation processes – or as we prefer to call them “workstreams” – have to be undertaken to ensure the seven key ingredients are in place. Figure 4.2 illustrates how the seven workstreams are linked to the seven key ingredients.

We have identified seven key workstreams:

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<tr>
<th>Workstream</th>
<th>Description</th>
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<tr>
<td>Selection of the Turnaround Team:</td>
<td>Appointment of a chief executive to lead the turnaround and selection of his or her direct reports.</td>
</tr>
<tr>
<td>Crisis Management:</td>
<td>Taking control of the distressed business and implementing aggressive cash management.</td>
</tr>
<tr>
<td>Stakeholder Management:</td>
<td>Rebuilding stakeholder confidence and reconciling their different interests within an overall recovery plan.</td>
</tr>
<tr>
<td>Develop the Business Plan:</td>
<td>The development of a detailed recovery plan for the business covering strategic, operational and organisational issues.</td>
</tr>
<tr>
<td>Implementation of the Business Plan:</td>
<td>The implementation of the detailed turnaround initiatives contained within the recovery plan.</td>
</tr>
<tr>
<td>Prepare and Negotiate Financial Plan:</td>
<td>Restructuring the capital base and the raising of the money to fund the turnaround.</td>
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<tr>
<td>Project Management:</td>
<td>The integration and co-ordination of the above six workstreams, ie overall management of the turnaround process (which is the overall management of the business).</td>
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Our experience is that in most turnaround situations the turnaround leader will have to undertake all seven workstreams although financial restructuring may not be required where the troubled company is a subsidiary of a healthy parent.

These workstreams are the essential implementation tasks of the turnaround process. Together the workstreams address the priority issues of managing the immediate crisis, fixing the operations, managing the various interests of those with a stake in the company, and ensuring that the company has sufficient cash to survive in both the short and long term.

Clearly a diagnostic analysis phase must be commenced first because the company doctor cannot cure the patient unless he or she knows what is wrong. However, in many situations it will be crucial to commence other workstreams in parallel with the diagnosis, particularly, in stakeholder interface management and crisis management. One of the priority actions for the newly appointed turnaround leader is to advise the stakeholders of his appointment and explain how he intends to tackle the situation. On day one the discussion may be limited to an explanation of the process he intends to follow. Such early initiatives start to rebuild confidence, demonstrate management control, and can help prevent the stakeholders taking any adverse action prematurely.
The other immediate priority is crisis management. The turnaround leader needs to rapidly assess whether the company has sufficient cash to survive in the short term whilst he carries out his diagnostic review and starts to formulate the recovery plan.

The analysis phase typically lasts between one week and three months depending on the size and complexity of the problem. During the later stages of the analysis, the turnaround team will have already started developing the detailed business plan. Our approach to business planning is intensive; the plan is 'the bible' for the rescue. It sets out in detail the specific actions to restore the business to profitability together with associated trading projections. The process involves several interactions as each stakeholder inputs into the plan. How long this takes will depend on the size and complexity of the company but we would normally expect the plan to be fully developed within three to four months and much quicker in some cases. Even before the plan is finalised, implementation can commence. Many of the initiatives are 'no brainers' and can be implemented before the plan has been fully and finally approved. The implementation phase typically lasts between six months and two years, and typically comprises an emergency phase, a strategic change phase and a growth phase. The financial restructuring is probably the last workstream to get underway. The key input for the financial restructuring is the operating cashflow forecast and funding projections for the business; this is contained within the business plan. As soon as these projections have been finalised work can commence on restructuring the debt and equity and raising new money.

(a) Diagnostic Review

The very first task that a prospective turnaround leader will want to commence is an analysis of the situation. Variously described as a strategic review, diagnostic review, business assessment etc, this critical phase must be the first step in the turnaround process and has the following objectives:

- To establish the true position of the company from a strategic, operational and financial perspective.

- To assess the options available to the company and to determine whether it can be turned around.
- To determine whether the business can survive in the short term.
- To establish the stakeholders position and their level of support for the various options.
- To make a preliminary assessment of the management team.

In many situations the troubled company may be rapidly running out of cash and the priority is therefore to move as quickly as possible through this phase. The approach is likely to be ‘quick and dirty’; analysis is high level, broad in scope, and in-depth only with respect to the key issues.

The diagnostic review needs to combine the elements of a conventional strategic and operational review with those of a corporate recovery/insolvency analysis. The team carrying out the review will therefore use traditional consultants methodology: the strategic and operational review will cover both the internal and external environment with a view to establishing the causes of decline and possible recovery strategies. The financial review will focus on establishing the current financial position and future trading prospects.

The review will need to consider the various options available to the company which are typically – sale of part/all of the business, turnaround, insolvency or closure/liquidation - and evaluate the financial outcome for the stakeholders under each scenario.

The techniques for the review phase follow conventional consulting methodology ie analysis of financial and operational data, interviews with management and staff, tour of facilities, discussions with suppliers, customers and industry experts, industry and competitor analysis.

At the end of the diagnostic phase the turnaround leader must have concluded as to whether turnaround is a viable option, the outline shape of the turnaround plan (and the approximate level of funding to support it) preliminary management changes and the extent of stakeholder support.

At the beginning of the analysis phase the prospective turnaround manager may not have taken a formal management position with the troubled company. At
this early stage, it may not be apparent as to whether turnaround is a realistic option or not. However, within a relative short period of time (a few days to a few weeks) the proposed CEO must decide whether to take on the turnaround assignment or not. Having made this initial decision the turnaround assignment can begin in earnest, and the turnaround manager can move quickly to commence crisis management and stakeholder interface management workstreams.

(b) Crisis Management

As soon as the turnaround option has been decided for the distressed company, crisis management should commence forthwith, if necessary; even before a turnaround manager has been appointed. Where this is the case interim management or consultants can be brought in to deal with the crisis. The most likely cause of failure in the short term is that the business runs out of cash thereby preventing the wages, rent etc from being paid. The priority is therefore to establish the critical payments that have to be made in the short term to keep the company alive and determine whether the existing bank facilities together with short term cash receipts (such as debtor collections) will be sufficient to cover the critical payments. If the analysis indicates a funding shortfall, the turnaround manager must move rapidly to bridge the funding gap by arranging additional funding, pursuing aggressive cash realisation strategies and restructuring critical payments, wherever possible.

Simultaneously, the turnaround leader must move rapidly to take control of the organisation. The priority in the short term is to try and limit the scale of the continuing decline by focussing attention on the most serious and urgent problems. The key issue is to determine what factors, if any, threaten the survival of the business in the short term.

(c) Selection of the Turnaround Team

Ideally an appropriate person will be appointed to lead the turnaround – usually a chief executive – as soon as the turnaround process is triggered by one or more of the stakeholders. This may or may not be before a diagnostic review has been undertaken. If the diagnostic review has been carried out by consultants or
investigating accountants, their report is usually the trigger to appoint a
turnaround manager and/or begin crisis management. Changing the top team
may however take time: incumbents have to be assessed and where a
replacement is necessary the recruitment process can take several months.
Getting the right top team in place is usually a time consuming task for the
turnaround leader.

(d) Stakeholder Management

We have previously described the key elements necessary to obtain stakeholder
support. As stated above we strongly believe that stakeholder management
should commence forthwith. The duration of the process varies considerably but
our strong preference is towards a longer than a shorter duration. Experience
suggests that debt and equity providers like to remain closely involved at least
until the "patient" is almost fully recovered. In practice this is likely to be
towards the end of the implementation phase ie a duration of up to about
two years although in some cases this is much longer as in the case of
Brent Walker which went on for about six years. One certainty is that the
recovery path will not be smooth and uneventful. More likely the company will
experience continuing uncertainty and turbulence during much of the early
recovery period. It is much easier to retain the confidence of the stakeholders if
they are kept fully informed of both positive and negative developments.

(e) Develop the Business Plan

We believe that successful leaders of turnaround situations move very quickly to
commence the development of a business plan which sets out their rescue
strategy.

The conventional consulting model is followed. Problems are initially identified
during the diagnostic review. Further analysis will identify the underlying
cause(s) of the problem and from this one or more remedies are developed.
Clearly there is a natural link between the diagnostic review and plan
development workstream. In our experience the two have a 'parallel' relationship ie they are partly sequential and partly parallel processes. Clearly
recovery strategies cannot be developed until the problem has been satisfactorily
diagnosed. However turnaround initiatives for problems that have been rapidly diagnosed can be developed while analysis continues on other more complex problems.

We strongly believe in the development of a comprehensive business plan. The plan should clearly state the long term goals for the business (vision/mission) together with the chosen strategy for achieving those goals. The plan should clearly define the products or services offered by the company together with its chosen markets. The core business processes for delivering those products/services must be explicitly defined. The plans should contain a detailed programme of turnaround initiatives that together form the rescue plan. Each turnaround initiatives should be described in terms of responsibility, proposed action, implementation timetable, required resources, and proposed impact.

The number of initiatives varies according to the size and complexity of the organisation. The size and scope of each initiative may also vary from a major restructuring improvement (such as rationalise ten factories to four) to a more modest action such as the hiring of new design director. Clearly the larger initiatives may comprise a major project on a stand alone basis and thus involve a number of sub tasks. In our experience turnaround plans rarely comprise less than fifty recovery initiatives.

Finally, the plan should contain detailed financial projections for year 1 and higher level projections over a three to five year period. The plan forms the 'bible' for the implementation process over the next six to eighteen months. Managing the implementation of the plan becomes the key focus for the senior management.

(f) Implementation of the Business Plan

The focus during this phase is the implementation of the turnaround initiatives incorporated in the business plan. The implementation of the business plan becomes the principal role of senior management. Although it may appear simplistic, it is generally the case that if an issue has not been addressed in the
business plan, it should not be an issue for management during the implementation phase.

We believe that rigorous project management is the key success factor for implementation. The plan sets out a programme of prioritised actions with timing, responsibility, and planned impact. The implementation process employs conventional project management tools (Gantt charts, progress reports etc) to drive accountability; the priority is to get people/teams to deliver their initiatives on time and on budget. Progress against plan must be monitored on a weekly basis, key issues must be dealt with when they arise and next steps must be continuously identified. Action becomes the defining watchword for the implementation phase.

Management of the implementation process is driven by regular progress meetings supported by continuously updated rolling implementation reports. Ordinarily the co-ordination or steering group will meet on a weekly basis during the early stages; as the turnaround progresses the frequency of these meetings may become fortnightly or monthly. The focus for the meetings is the review of progress against each initiative.

(g) Prepare and Negotiate the Financial Plan

The business plan is the basis of the financial restructuring plan – if that is necessary. The financial projections accompanying the business plan will be from the basis of the cash flow forecasts which are the key input into assessing the future funding requirements of the business.

(h) Project Management

We have already mentioned the need for detailed project management of the implementation initiatives. However, the whole turnaround process needs project managing by the turnaround manager. He or she needs to fit the various parts of the turnaround jigsaw together: the turnaround manager has to be able to mesh the seven key ingredients together at different stages of the turnaround process.
The turnaround manager does not therefore have the luxury, enjoyed by many other participants in the turnaround, of being able to concentrate solely on one phase of the turnaround at a time. This is a difficult challenge for the turnaround manager as the objectives of each phase can be quite different. For example, the mindset and style required for crisis management is quite different from that required in business planning, yet these phases of the turnaround are managed side by side.

TIMING

The turnaround process is characterised by considerable overlap of the planning and implementation phases. We identify four distinct but overlapping phases in the implementation process:

- the analysis phase
- the emergency phase
- the strategic change phase
- growth and renewal (beyond turnaround)

Figure 4.3 illustrates how the workstreams discussed in the previous sectors are phased throughout the turnaround process.

Analysis Phase: This phase encompasses more than just the diagnostic review. We have already stated that stakeholder interface management and crisis management often need to begin in parallel with the diagnostic review and that the diagnostic review itself is the starting point for the development of the business plan. Thus we may begin to see some generic strategies – such as cash management, change of chief executive, tighter financial control – starting to be implemented in the analysis phase.
**Figure 4.3: Phasing of Workstreams Throughout the Turnaround Process**

<table>
<thead>
<tr>
<th>Analysis Phase</th>
<th>Emergency Phase</th>
<th>Strategic Change Phase</th>
<th>Growth or Renewal Phase</th>
</tr>
</thead>
<tbody>
<tr>
<td>Diagnostic Review</td>
<td>Crisis Management</td>
<td>Develop Business Plan</td>
<td>Financial Restructuring</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Implementation of Business Plan</td>
<td></td>
</tr>
<tr>
<td>Selection of Turnaround Team</td>
<td></td>
<td>Stakeholder Management</td>
<td>Project Managing the Turnaround</td>
</tr>
</tbody>
</table>

The emergency phase: The emergency phase consists of those actions necessary to ensure survival and therefore tends to focus on those generics strategies that can most easily be implemented in the short term. The distinction between implementation of the business plan and crisis management can become blurred. Thus, one finds cash generation, cost reduction, increased prices and increased selling effort as the principal generic strategies used in this phase of recovery. Organisational change to facilitate control and management, may take place.

The emergency phase is often characterised by surgery: divesting subsidiaries, closing plants, making employees redundant, firing incompetent managers, reducing surplus inventories, selling obsolete inventories, cutting out unprofitable product lines, etc – all actions designed primarily to improve the cash outflow and stop the losses.

It is during the emergency phase also that the firm may seek additional financing to implement its recovery strategy and therefore there is overlap with the financial restructuring workstream. The emergency phase will, typically, last from six to twelve months, but longer if appropriate recovery strategies are not adopted or are not well implemented.
The strategic change phase: Whereas the emergency phase tends to emphasise operational factors, the strategic change phase emphasises product-market reorientation. By good implementation of an appropriate recovery strategy in the emergency phase, the firm has assured short-term survival and can begin in the emergency phase to focus strategy on those product-market segments where the firm has most competitive advantage (usually, but not always, those segments where it is profitable). However, product-market change usually takes time to implement and may require some investment, which may not be possible in the early phase of recovery. It is at this strategic change phase that management and/or shareholders may realise that the long-term viability of the firm looks doubtful, or that the investment of money and time required to achieve sustainable recovery is not worth the risks involved. They may, therefore, decided to look for a suitable purchaser for the business.

Assuming product-market reorientation appears viable, the strategic change phase is also characterised by:

- An increased emphasis on profits in addition to the early emphasis on cash flow. Return on capital employed is still unlikely to be satisfactory at this phase, although losses have been eliminated.

- Continued improvements in operational efficiency.

- Organisation building – which may be important, bearing in mind that the organisation may have been traumatised in the emergency phase.

One US writer refers to this phase as one of stabilisation, because the organisation needs time to settle down and prepare for a phase of renewed growth. New management will probably have brought with it a new organisational culture which will take time to become institutionalised. Stabilisation is important, yes; but alone it is insufficient to give the firm a sound base for the future. That can only be accomplished by refocusing the firm’s product-market position or sharpening its existing competitive advantages.

The growth phase: Before this can begin, the firm’s balance sheet must have improved. Once it has the firm can start to grow, either organically through new product
development and market developments, or via acquisition or both. This is the final phase of the turnaround process and the beginning of which is sometimes called corporate renewal. However, in some industry sectors, such as high technology, a rapid return to growth maybe a pre-requisite for a successful turnaround.

CHARACTERISTICS OF SUCCESSFUL RECOVERY SITUATIONS

There are substantial differences between the recovery strategies adopted by successful turnaround leaders and those that are not. Successful recovery situations are characterised by:

- Rescue plans that incorporate the seven essential ingredients. A very common source of failure is to initiate too narrow a turnaround. The turnaround leader has to not only manage the immediate crisis and tackle the strategic and operational problems of the business, but also rebuild stakeholder confidence and ensure the company has adequate funding for the future.

- An approach that addresses the key issues simultaneously rather than in a linear sequence. In the early days, the turnaround leader should start the process of rebuilding stakeholder support in parallel with the early stages of managing the crisis and developing the business plan.

- A rescue plan that is broad in scope, ie it tackles cost reduction and revenue growth, deals with hard and soft issues, incorporates strategic and operational initiatives and addresses both short and long term priorities.

A study comparing successful and unsuccessful turnaround efforts undertaken by one of the authors in both the UK and USA showed that successful turnarounds are characterised by:

- management changes, particularly the appointment of a new chief executive and a new financial director

- the use of multiple cash generating strategies

- improved financial control systems that are really used by management to install a performance orientated culture
an understanding that cost reduction strategies although important are usually insufficient to effect a successful turnaround

fundamental product-market reorganisation is usually necessary alongside improved operational marketing

significant organisational change in terms of structure processes and improved communications

Two key messages stand out in examining successful turnarounds. Firstly, successful firms use twice as many generic turnaround strategies as unsuccessful firms: they undertake a lot of generic strategies in parallel. And secondly, they implement more vigorously. There is nearly always a need for more rather than less actions. We see this in practice when the initial turnaround manager is replaced because he or she is failing to make a real financial impact within the first 12 months. The replacement turnaround manager will always use more strategies and implement those of his or her predecessor more vigorously.