

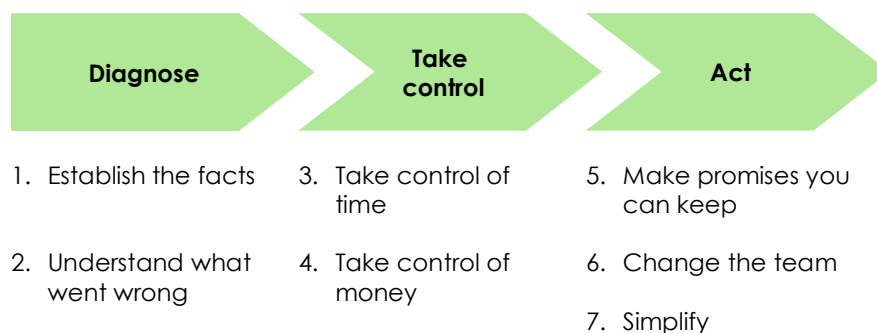
Successful Turnarounds

The definition of a turnaround is very broad. It is basically about improving performance from bad to good. At one extreme, turnaround stories are about turning an under-performing company into a world-beater; using sports language, taking a regular team player and turning him into the world champion. This article is about the other extreme of getting the regular athlete out of intensive care: taking a company that will not survive in its current form to a position where it is profitable and sustainable.

Using this definition, most turnarounds do not succeed. The majority of respected surveys put the success rate of turnarounds between 20% and 35%, depending on the definition of underperformance and success. Those with turnaround experience know also that they are usually highly stressful and, if unsuccessful, very poorly rewarded.

We believe that it does not have to be this way. In our experience, there is almost always a decent business in amongst the detritus of a struggling company; which a smart CEO can rejuvenate with some tough decisions and a close eye on the business.

We work with some outstanding turnaround CEOs, whose success rate is close to 100%, and whose approaches share a series of common measures, which we summarise below. This list is not meant to represent a guaranteed recipe for turnaround success, it does not reflect the importance of addressing the specifics of each unique situation, and by definition it is incomplete. It is nevertheless a set of simple actions common to all the successful turnarounds we have witnessed and supported. We describe these measures in the broad order in which we observe them:



We have written this article from the perspective of the new CEO. This is because we believe that a new CEO, brought in or promoted internally, is pre-requisite for getting a company out of intensive care or creating any step change in company performance.

1. Establish the facts

It is an almost universal practice and requirement for turnaround and recovery experts to establish the short term (three to six months) viability of the business. This is typically a rapid, internal exercise focused on contracts, commitments and cash flows. The exercise is absolutely necessary, but sufficiently well-understood and common that we will not cover it further.

Less common, but equally vital is ascertaining the one-year viability and two-year potential of the business.

This exercise is not a luxury: successful turnarounds almost always require liquidity from either debt or equity; and these sources will need to be reassured that there exists a viable business in the mid term, and that they are not throwing good money after bad.

The work requires an investigation of commercial reality, looking both inside and outside the business.

- Externally, it requires interviews at a micro level to understand as clearly as possible customers' budgets and spending intentions, and research at a macro level to garner the full facts of relevant market trends and competitive developments
- Internally, it requires a robust analysis and understanding of sources of profit and loss by either product, customer or market

The entire exercise can take as little as two to three weeks for an experienced team, can be performed with minimal disruption to the business and if done well forms the basis of evidence for the recovery strategy. Armed with genuinely solid and accurate information about the external and internal business reality, the recovery strategy is rarely complex and generally obvious.

It is rare that we look beyond two years in distressed or turnaround situations. The time to look at outer years is when the fires are mostly out.

2. Understand what went wrong

Companies we support in turnaround find themselves there for two generic reasons: either something major went wrong for a short time, usually loss of a dominant customer or a dramatic market change; or something minor went wrong for a long time, usually poor understanding of customer or product profitability, that led to misguided allocation of capital and resources. Either way, the reason for the problem needs to be flushed out and addressed. Any recovery plan is simply not credible without this process. In our experience, the forensic exercise to find the source of the problem is rarely difficult for fresh eyes.

It is tempting to blame market changes when things go wrong, and we hear this all the time. Sometimes market downturns do happen unexpectedly and these can land the company in trouble. So the company was unlucky. That doesn't matter – the turnaround doesn't hang on whether anyone was to blame or whether they were battered by fortune. What matters is that we need to establish whatever went wrong and fix it.

3. Take control of time

Senior teams, and particularly CEOs and finance teams, in distressed or turnaround situations, experience relentless demands on their time from all sides: owners, owners' advisors, banks, banks' advisors, customers, creditors, worried employees, worried Board members; the list goes on. At the same time, management is constantly harried by a series of apparently urgent tasks, each of which appears to be critical in its own way.

Tempting though it may be to heroically charge from fire to fire, coming up occasionally for air to report to lenders or answer questions from advisors; the senior team cannot possibly effect any sort of successful turnaround in such a responsive way.

The CEO needs to create breathing space for the business.

From our observation, the first thing successful turnaround CEOs do to achieve this is take control of time. They understand the requirement to accommodate communication needs and put out the urgent fires; but they also recognise the crucial necessity to protect the time that they and their team need to think, understand the problems in the business, formulate the plan, delegate and implement it. This protection takes numerous forms, such as establishing regular update meetings with all parties to limit repetition, setting weekly time aside to plan or talk to key customers; whatever it takes to promote the important so it is on par with the urgent.

4. Take control of money

Equally important to taking control of time is taking control of money, understanding where every pound is going and coming from. It goes without saying that the CEO needs to take decisive action on business solvency and a plan to return to profitability, which most usually means addressing cost. Where successful turnarounds differ is in the management of details, and the corresponding flows of money. The most effective turnaround CEOs we know make a habit of establishing and monitoring a realistic pipeline, creating a bottom-up budget and making the team accountable for every pound of income and spend.

In addition to problems of solvency and profitability, most companies in turnaround situations have issues with liquidity. Whereas profitability can be addressed internally by sensible planning and performance management, liquidity usually requires external support from financiers, ranging from payment holidays through to cash injections.

This liquidity brings breathing space that allows management to make calm, rational decisions that support long term survival and profitability. Without it, the company can end up in a frenzied cash and business chasing environment, of constant triage with an eye only on today's problems.

The senior team has numerous tools at its disposal to persuade financiers or creditors to extend liquidity: the CEO's personal turnaround track record, the business pipeline, the bottom-up budget, evidence of future customer spend or market growth, a plan to address what went wrong. But management's strongest card, and now a regular requirement from lenders, is to make the liquidity conditional, i.e. making continued or extended financing subject to hitting a number of agreed goals. We cover this next.

5. Make a series of promises you know you can keep

At the start of a turnaround every party with an interest is worried: employees, shareholders, banks, creditors, business partners, customers and suppliers. Increasing their confidence is critical to making any progress.

It is in management's interest to be proactive and make a series of promises, which it knows it can keep. Hitting these checkpoints is the most effective tool management has to build its credibility. The most basic, and likely required, is a revised budget, but other forward-looking checks are also helpful. With every check management hits and promise it keeps, it builds credibility and confidence, financiers become less stringent

and heavily involved, customers and suppliers go back to their regular relationship with the company.

To be successful, this approach naturally works its way down the organisation. For the CEO to promise a series of financial achievements to investors, he needs to be confident that his team can deliver on their promises in each of their areas, and so on. This approach also has enormous and innate internal benefits - hitting promises helps organisational self-belief when the company needs it most.

The most important characteristic of such promises is not that they are ground-breaking, but that they are achievable in short time. As the mantra went in IBM's turnaround "win small, win early, win often".

6. Change the team

We have never seen a dramatic change in the fortunes of a company without a corresponding change in the senior team. This means at least two or three changes in senior personnel, almost always including the CEO.

It is usually self-evident, and often self-selecting, who is engaged in the turnaround and who wants out. We believe it is the job of the CEO to check the attitude of each member of the team and make the decision quickly. We have yet to come across a successful turnaround CEO who has regretted changing the team or has said they did it too quickly. We also find that getting the right turnaround team together is predominantly a matter of attitude; aptitude rarely comes into it.

7. Simplify

Complexity is a double-edged sword in turnarounds. Companies often get into trouble when they have taken on too much; and when they are in trouble they try extra things to get out of it.

By definition, many of these are not working and at best create a mass of distraction that the business can do without.

When cash and time and goodwill are constrained, the business needs to concentrate on doing a small number of things well. This can mean reducing product lines, cutting or selling business units, outsourcing business processes or numerous other simplifications depending on the situation. Whatever is done, the process of simplification needs to go far enough to give the remaining activities the focus of management time and investment required to do them well.

All of these things are common sense and relatively obvious, but all of them are also easy to duck or delay. Hopefully, this article illustrates that our clients that have performed successful turnarounds simply do the sensible things that experienced managers know they should be doing anyway.