The Three Steps of Successful Turnarounds

When companies find themselves in distress, turnarounds are one way to set them back on track. But turnarounds are messy and getting them right is no easy task.

It was November 2010 when Sankar Krishnan, managing director at the global professional services firm Alvarez and Marsal (A&M) and Nikhil Shah a senior director of the firm were called in to investigate claims of irregular activities allegedly involving the senior management of a textile manufacturer in India. As we detail in this INSEAD case study, the seriousness and potential impact of the allegations from a former employee meant they had to tread very carefully. They decided on a covert operation, since it was unclear who was trustworthy at the company and given that a direct approach might have led to evidence being destroyed that could be crucial to the investigation.

After a corporate investigations firm did an initial check and found some substance to the allegations, Shah and Krishnan decided that they first had to mount a swift takeover of the top management to get a handle on the business and the allegations. Krishnan assembled an interim management team and a forensic team to conduct investigations.

After meticulously planning every step of the takeover, the company’s CEO and CFO were invited to what they thought was a regular board meeting. They were immediately suspended, along with three other senior managers implicated in the accusations.

An interim Alvarez & Marsal management team was sent to the company’s headquarters, where they realised the full extent of the task ahead: plant equipment was obsolete; costs of raw materials were soaring; the brand was tired; long overdue payments were coming in at irregular intervals; there was no systematic or scientific inventory management. The challenge was multifaceted and daunting.

Over the years, Krishnan and Shah have implemented successful turnaround strategies in many struggling companies around the world. This particular case was no exception – in fact they assured me it was far from being their most challenging they had seen in their professional careers. In an interview on the case study of this turnaround, I asked them how they start when they first enter a turnaround situation and how they get a company back on its feet.

Getting to Grips with the Situation

“Cash is king”, Krishnan explained. “The first thing you want to do is get to grips with the liquidity of the business. This entails finding out exactly where cash is coming from, how much is coming in, how much is going out, and figuring out how to maximise incoming cash flows. This is crucial, since it ensures that there is enough cash to keep the business
going, and buys management time to think ahead and gives them space to maneuver.”

The second step according to Shah is to determine where operational improvements can immediately be made. “We usually try and identify which aspects of the production process can be improved, and where productivity gains can be made. Where possible we also try to identify where wastage can be reduced, and search for better suppliers.”

Finally, the third step entails implementing the short-term turnaround plan. Shah and Krishnan typically spend the first 30-60 days designing a plan around what the business drivers should be going forward, taking into account the stakeholder issues, customer issues and potentially new methods to introduce to improve processes.

However each case is unique, and while these methods are broadly applicable to most cases, there are other company- or country-specific factors that must be taken into account.

Dealing with Stakeholders

Local culture (whether company culture or national culture) is one such factor. In the US, the top-down approach and fast decision-making style sits well with managers and employees; plus the court system is strict and bankruptcy procedures are orderly. “You are then working with secured lenders who really have control of the company” said Krishnan.

But in markets such as India, “upward of 70 percent of the businesses are owned by the founder so you have to have a very consensual agreement with the promoter…we may have the title of “chief restructuring officer” but if we can’t work with or through the CEO or the chairman, nothing will get done”.

Employees, suppliers, creditors and customers add to the complexity of executing a turnaround. “It’s very, very important to over-communicate in these situations. You have various stakeholders who can all put a stop to what you’re doing if they want to. Over time, once you build up the confidence and credibility with them, everyone starts moving in the right direction. But in the beginning communication is critical,” said Shah.

Communication is one of the key skills companies like A&M look for in the people they hire. Shah and Krishnan also share that analytical capability, objectivity and the ability to build consensus are essential skills to make a career in the turnaround industry. The ability to carry people and sell the plan can be adapted to most situations despite the varying degrees of distress A&M consultants find themselves involved in.

Warnings signs - The Writing on the Wall for Companies

In their experience, Shah and Krishnan point to a few key warning signs that a business is heading for distress. First, when an organisation expands into areas that distract it from its core business, capital and resources can be allocated to the wrong places and cause its cash flow to dry up. Krishnan cites the story of two brothers who ran an ink-manufacturing company. They decided to go into the aircraft leasing business and ended up losing €120 million. Secondly, expanding into unknown geographies without enough preparation or understanding of local conditions, which can often cause debt to build up and cash generation to suffer. Thirdly, assuming that things don’t need to change as long as the company is generating revenue. There are always things that can improve, from cash flow to operational efficiency. Companies that have become complacent are often those that end up in turnaround situations.

Claudia’s three key ingredients to turnaround success, from her MBA elective “Managing Corporate Turnarounds”, developed jointly with her colleague Joost deHaas

1. Diagnostic Review: Conduct an assessment of the current and future business situation from a cash flow perspective, to gain a clear idea of the performance improvements needed and (most important) the time available to achieve those results. Conduct a forward looking 13-week cash flow projection (at times done daily in critical situations). This is a critical first step in this process and at times an invaluable tool for the company to stay afloat throughout the Turnaround.

2. Turnaround Tools: Clarity of the tools available to improve operational & financial results fast is crucial and the Turnaround team will draw especially on short-term value creation levers. How to make the best use of our “Turnaround Toolbox” is the main focus of the class

3. Turnaround Team: Decides quickly and decisively, being better roughly right – than exactly wrong since time is of the essence. The team ensures effective communication (internal & external) and manages the relationship with key stakeholders (customers; creditors; suppliers etc …)

Our course - Managing Corporate Turnarounds
is one of the capstone electives in the INSEAD MBA programme. Taught in the final period of the MBA, it gives our students an opportunity to apply their learnings from the last year and combine their expertise to “rescue” companies, engage with Turnaround CEOs & professionals like Sankar & Nikhil from A&M and finally to get their hands dirty in our Turnaround simulation; this is a weekend-long bootcamp where student teams attempt to rescue SAAB, the venerable car-brand that went through bankruptcy in 2010. It goes without saying that the course became quickly one of the most popular courses in the INSEAD MBA programme, when we launched it 6 years ago.

My premise at the start is simple: When the times are good, (almost) anyone can lead a firm, but when the storm hits and a company starts down the slippery slope into distress, the rules change completely:

Management’s focus changes to cash, cash and cash, simply the most important consideration for a company in trouble. Recovery and survival become the strategic priorities, which means not only juggling the demands and perceptions of clients, employees and pushing creditors and suppliers but also communicating progress and at times painful decisions in a clear and timely manner is critical. Of course the pressure of time in addition to regular business demands makes all these actions that much harder and puts a tremendous strain on management.

The case study, "Crisis at the Mill: Weaving an Indian Turnaround - Alvarez & Marsal" won the Indian Management Issues and Opportunities category at the 2015 EFMD Case Writing Competition.

Claudia Zeisberger is a Senior Affiliate Professor of Decision Sciences and Entrepreneurship and Family Enterprise at INSEAD and the Academic Director of the school’s Global Private Equity Initiative.

Follow INSEAD Knowledge on Twitter and Facebook

Find article at https://knowledge.insead.edu/blog/insead-blog/the-three-steps-of-successful-turnarounds-4202

Download the Knowledge app for free

Visit INSEAD Knowledge http://knowledge.insead.edu