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Facilitators and Inhibitors of Supply Chain Innovation-prospects for Supply Chain Managment in the Irish Grocery Sector

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COMPANY TURNAROUND STRATEGIES: A CONTEXT FOR MARKETING

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Summary

This article considers the literature on corporate turnaround. It examines the nature of decline as well as the causes and the various indicators of decline. Following this Hofer's now well-established framework of analysis for the development of a turnaround strategy is described. This analysis falls into two stages: firstly, an assessment of current operational and strategic health of a firm and secondly, a consideration of turnaround options which may incorporate strategic and/or operational change. This model is then assessed in the context of a number of Irish firms in a turnaround situation. Important issues in turnaround strategy, such as management change, financial re-structuring and strategic realignment are addressed. In particular, the role and importance (and indeed, sometimes the unimportance) of marketing in strategic realignment are considered.

Strategic analysis has traditionally implicitly focused on companies in a healthy condition contemplating growth or development strategies. But over the last ten years, a body of literature has developed in the area of strategic analysis focusing on companies in difficulty with a view to turning such companies around. A number of works have emerged on the topic of company turnaround, significant amongst them being contributions by such authors as Bibeault,[1] Argenti,[2] Slatter,[3] and Kharbanda and Stallworthy[4]. One particular contribution, that of Hofer,[5] offers an exceptionally interesting perspective and develops a framework which identifies important management and strategic marketing issues in the analysis of turnarounds.

This article considers briefly the literature on corporate turnaround. It examines the nature of decline as well as the causes and the various indicators of decline. Following this, Hofer's framework of analysis for the development of a turnaround strategy is described. This analysis falls into two stages: firstly, an assessment of the current operational and strategic health of a firm and secondly, a consideration of the turnaround options which incorporate strategic and/or operational change. Hofer's framework is then assessed in the context of a number of Irish firms in a turnaround situation. Important issues in turnaround strategy, such as management change, financial re-structuring and strategic realignment are addressed. In particular, the role and importance (and indeed, sometimes the unimportance) of marketing in strategic realignment are considered.

Corporate Decline and Turnaround

The analysis of company turnaround usually starts with an analysis of the factors which have caused the decline. But this of course, presumes a clear cut definition of the nature of decline. Schendel, Patton and Riggs define decline in terms of performance of net income earned and also turnaround in similar terms.[6] Decline by their definition is regarded as having taken place if there are four years of uninterrupted decline in net income as normalised by GNP growth. Recovery is defined as having taken place if there are four years of increase in net income with allowance for a two year deviation between the downturn and upturn phase. Again net income is normalised by GNP growth. Hambrick and Schecter in their study of short run turnaround, using the Strategic Planning Institute's profit impact of market strategy (PIMS) data-base, looked at firms whose ROI recovered from less than 10% (pre-tax) to more than 20% (pre-tax) over a period of four years.[7]

Without becoming embroiled at this stage in setting down a precise definition of decline, it is worth considering more general factors which indicate decline and trigger the need for a turnaround strategy. In this vein Hofer considers the context in which turnarounds are necessary and pursued.[8] He argues for two important dimensions to the context: firstly, the areas of organisational performance affected and secondly, the 'time criticality' of the turnaround situation.

Poor organisational performance may be reflected in three different ways:

- Decline in organisational efficiency and/or profitability

- Lack of growth
- Poor asset utilisation

The notion of assets in this context might be usefully broadened to include marketing related assets such as brand image or market share. Indeed a number of recent takeovers and mergers on a transnational basis in the European Community reflect a realisation by acquiring companies that firms with under-utilised marketing related assets, such as brand names, corporate identity, market share and so on, are very worthwhile acquisitions.

The second characteristic of turnaround situations that is important to the design of effective turnaround strategies is the time criticality of the firm's situation i.e., if the situation is very critical, more readily deployed operational change may be more useful than long term strategic change. The reason for this is the lengthy time delay that usually exists between the taking of strategic action and the response that accompanies it. When the threat to organisational survival is not imminent — when there is some time to respond in a variety of ways — then it is possible to 'tailor' the turnaround strategy to the specific situation involved.

Cause of Decline

While there is variance in the precise definition offered by different authors, it should be borne in mind that agreement regarding the definition of decline is not central to the analysis of corporate decline and turnaround. If decline is apparent by whatever definition of decline chosen, it is possible then to examine the causes of decline. Slatter compares a diversity of classification of the causes of decline (Figure 1).[9] In all of these classifications, inadequacy of management appears as a causal factor in decline. But the definition of inadequate management is often loose and, more importantly, other factors cited are, of course, a consequence of inadequate management. Bibeault, like other commentators, identifies poor top management as a major cause of decline and goes some distance towards defining inadequate management.[10] He argues that poor management may exist because of:

- Incompetence of people at the top
- Narrow vision of managers
- Displacement activity — either too high or low a turnover of managers

While this hardly constitutes a comprehensive definition of management inadequacy, Bilbeault does develop the concept further and offers some interesting observations on this problem, not of immediate relevance to this discussion.

Indicators of Decline

An important distinction in the analysis of the decline must be made between the causes of decline and the symptoms of decline. Traditionally the most common symptom used in identifying organisation decline relates to financial ratio analysis. John Robertson has evaluated the traditional ratios used by organisations to measure their financial health.[11] He finds that the profitability ratios can be misleading, while the liquidity ratios are not responsive to changes taking place in the working capital cycle of failing companies. On profitability ratios he finds that the traditional ratio of ROI incorporating sales/net operating assets can be misleading and that sales/total assets is a much better ratio to use. In his research, Robertson looks at the balance sheet of failed organisations over the five previous years to failure and applied the traditional ratios to them. He concludes that there are major shortcomings in traditional ratios as predictors of failure. Robertson subsequently develops a model which he argues would have predicted 87% of the failures in forty-eight failed organisations at least two years in advance of a significant deterioration in their financial health. Altman's well known Z-score approach also consists of a a composite of ratios but Taffler[13] argues that the precise Z-scores to be used as warning indicators would differ from country to country and industry to industry. Bibeault emphasises the importance of declining margins and other non-financial indicators such as management turnover

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in conjunction with traditional financial indicators as predictors of decline.[14]

Handy indicates some corporate cultures as being more susceptible to crisis than others, although no single cultural pattern leads to crisis.[15] This author found in his research that both bureaucratic types of culture (firms governed by rules and procedures) and firms exhibiting power cultures (e.g. the one-man-show type organisation) appear to be most susceptible to crisis. But it can be argued that Handy's definition of culture is somewhat primitive compared to recent developments of the concept of corporate culture.

Figure 1

Causes of Corporate Decline

Slatter	*Argenti*	*Schendel, Patton & Riggs*	*Sigoloff*
Lack of financial control	Accounting information		Lack of control
Inadequate management	Management	Management problems	Peter Principle Management without guts International conflict at decision-making level
Competition	Firm unresponsive to change	Increased competitive pressure Lower revenues	Change in technology Firm hostage to current product-markets
High cost structure relative to competitors		Higher costs	Development of locational disadvantages
Changes in market demand	Normal business hazards	Demand declines	Change in marketplace Increasing cost of debt
Adverse movement in commodity markets (including interest rates)			
Operational marketing problems		Marketing problems	Poor distribution
Big projects	Big project		Dependence on single customer
Acquisitions			
Financial policy	Gearing		Limited financial resources
Overtrading	Overtrading		Sales growth faster than working capital
		Strikes	

Source: S. Slatter, *Corporate Recovery: Successful Turnaround Strategies and Their Implementation,* Penguin Books, London, 1984, p. 26.

Large organisations may well be prone to failure as they are likely to have developed a sophistication in management which embodies sensitive environmental scanning and internal control systems that identify problems at an early stage, thus resulting in corrective action. Williams in a study of failure in large organisations identifies distinctive problems in such ailing organisations.[16] For example, he argues that failure often follows a period of expansion largely financed by debt. The identification and correction of difficulty may be inhibited by psychological pressures as executives who have enjoyed driving their organisation vigorously forward find it very hard to shift into low gear or reverse.

Assessing Current Operational Health

A first step in the development of a turnaround strategy is obviously an analysis of the current situation. Hofer argues that this analysis can be divided into two main areas of examination — an analysis of the current operational health and an analysis of the current strategic health of the organisation.[17] Organisational operational health may be assessed by examining four main areas.

Financial Condition: Indicators mentioned earlier such as Altman's Z-scores or other composite ratios may be used to assess how near the firm is to bankruptcy given the continuation of current strategies or to indicate the financial resources that could be raised in the short term to aid the battle.

Market Position: An assessment in this area would focus on the possibility of increasing sales within the present product/market scope to improve financial performance. Struggling firms rarely have the resources to successfully introduce new products.

Technological Stance: Generally product innovation should receive little attention due to the foregoing factors, but an assessment of the quality relative to the competition of the firm's products should be made. This may indicate, if quality is good, possibilities for increasing prices.

Production Capabilities: Critical here will be the variable cost position of the firm in relation to its competitors. It will also be necessary to establish what facilities absolutely need to be replaced to continue business in the short term and what facilities might be sold off.

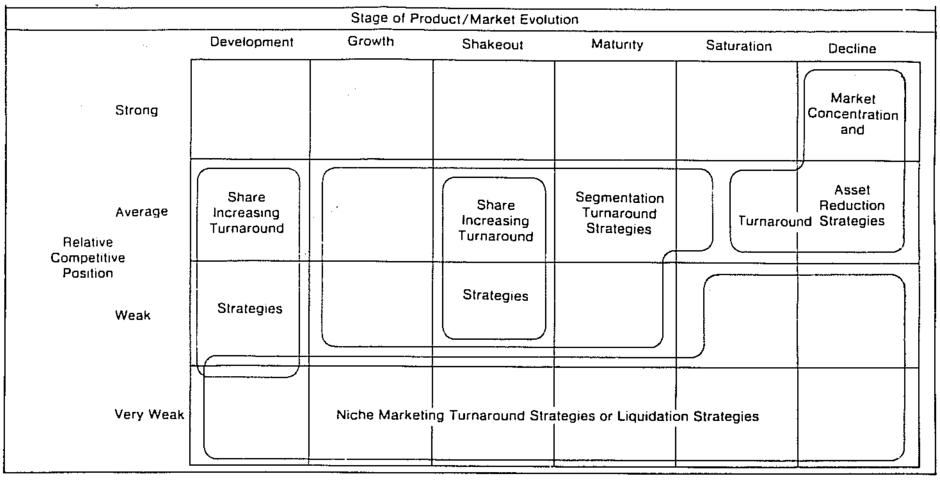
The above framework of analysis is very straightforward in its approach, paralleling the functional structure and activity of many organisations. It does not explicitly examine the personnel function and management capability, or more accurately its absence, which is reflected in performance in the functional areas. Since Hofer's original development of this framework almost ten years ago, a wide variety of measures have been developed both on a functional basis and on an industry basis to assess operating performance. For example there are well established criteria in the area of marketing. If we consider sales activity, measures of performance such as sales force productivity, advertising effectiveness and distribution effectiveness are strongly established areas of control in operational marketing activities. In the production function, most industries now have available a wide variety of criteria of performance that relate specifically to the industry concerned. For example, in electricity utilities there are criteria such as thermal efficiency of generating plant, million kilowatt hours sold per employee and fuel cost per unit sold.

Assessing Current Strategic Health

Similar dimensions to those used in assessing operating health can be utilised in assessing strategic health. Again Hofer argues for four dimensions in the analysis and suggests a useful matrix as a tool of analysis and as an indicator of the turnaround strategy to be chosen.

Market Position: The first aspect to be examined is market position. A six-by-four matrix with market evolution and relative competitive position on respective axes offers a classification of possible turnaround strategies (Figure 2). A criticism of this model is that the recommended strategies could apply equally to healthy companies at any of the stages of the industry/product-market evolution as they would to companies in difficulty. The recommendation of a niche strategy for companies in a very weak relative competitive position suffers from the same deficiencies as the general recommendation by niche enthusiasts for healthy companies or new companies, i.e., it constitutes a form of escapism from normal competitive forces and presumes that these will not ever exist in the niche or at least not until the first entrant has established a strong position. This may not always be the case.

Figure 2
Assessing Current Strategic Market Position



Source: C.W. Hofer, "Turnaround strategies", *Journal of Business Strategy*, vol. 1, no. 1, 1980, p. 22.

Technological and Production Capabilities: The analysis of the company's competitive position here will obviously be a function of the nature of the industry and the stage of industry evolution. For example, firms competing in mature industries will be concerned with process R & D, whereas firms in emerging industries will be concerned with product R & D.

Finances: Hofer makes the case that finances are inconsequential in that in the long term they will take care of themselves if the business is healthy in terms of markets, technology and production facilities, while admitting that in the short term, certain adjustments may have to be made to allow the firm to continue to exist and to take remedies in the other functional areas. This probably understates the extent to which significant capital restructuring may be an essential ingredient to both short term and long term recovery.

Selecting the Type of Turnaround
The type of turnaround strategy that should be selected by a firm will depend on its current operating and strategic health. If both are weak, then liquidation is probably the best option unless the firm has no other business it could invest in; in this case a strategic turnaround with tight controls may be possible. With a weak operating position and a moderate or strong strategic position, an operating turnaround strategy is usually advisable. When the business is strong operationally but weak strategically, then a strategic turnaround is almost always indicated though the firm may have a period of grace to decide what it will do. When both operating and strategic health are strong, turnaround strategies are seldom needed unless it is to improve asset utilisation which may sometimes lag.

Strategic turnarounds focus on change in strategy; performance is seen as a derivative of chosen strategy changes. "Strategic turnarounds can be divided into those that involve a change in the organisation strategy for competing in the same business and those that call for entering a new business or businesses".[18] Operating turnarounds focus primarily on performance targets to be achieved. Hofer identifies four general types of operating turnaround strategies, none of which require change to the firm's strategic posture. These are:

- Revenue-increasing strategies
- Cost-cutting strategies
- Asset-reduction strategies
- Combination strategies

In practice the distinction between strategic and operating actions in turnaround can often become blurred. Thus, actions that substantially decrease the firm's asset base, also often require a change in strategy to be most effective. However, even with this limitation the distinction is still relevant because of different priorities, trade-offs and time scales associated with the two levels of decision-making.

Other authors suggest different approaches to selecting the type of turnaround required. Slatter, for instance, identifies ten generic strategies.[19]

- Change of management
- Strong central financial control
- Organisational change and decentralisation
- Product-market re-orientation
- Import marketing
- Growth via acquisitions
- Asset reduction
- Cost reduction
- Investment
- Debt restructuring and other financial strategies

Further, Slatter points out that the selection of the appropriate generic action at strategic and/or operational level is a function of the actual causes of decline. Taking Slatter's[20] classification as a point of departure Figure 3 develops a framework of relationships between causes of decline and appropriate remedial activity which offers important additional causal factors and remedial activities; it also distinguishes remedial activities along strategic and operational dimensions.

Figure 3

Causes of Decline and General Remedial Activities

Causes of Decline	*Principal Remedial Activity*
Poor Management	New Management‡ Organisation structure change‡ Change in organisational culture‡
Over-diversified	Retreat to core business*
Poor operational marketing	Appropriate improvements in promotion, selling, distribution, etc.†
Competitive weakness	Change in strategy* Changes in operational areas which have caused competitive weakness†
Financial difficulties	Improve financial control† Capital restructuring*

* involves mainly strategic change
† involves mainly operational change
‡ involves both strategic and operational

An Exploratory Study of Irish Companies

The sample of companies chosen in this study was drawn from turnarounds in the Top 500 Irish Companies. Given the structure of Irish industry, which includes a high proportion of foreign companies (they account for approximately 40% of industrial employment) only indigenous companies were selected as decision-making in multinationals is often not located in the host country. From a total of twenty turnaround situations identified, six were selected on the basis of willingness to participate and also on the basis of discussion with Foir Teoranta, the state finance company charged with the responsibility of acting as a financial rescue agent to companies in very severe difficulty. The companies are briefly described in Exhibit 1.

Exhibit 1

Company Profiles

Company	*Pre-Turnaround Employment*	*Product Area*	*Ownership*
British & Irish Steam Packet Company Ltd. (B&I)	1000+	Sea transport	State
Bewleys Cafes Ltd	<500	Food whole-saling and catering	Co-op
Arklow Pottery Ltd.	500+	Tableware	Private Ltd. company
Great Southern Hotels	<500	Hotel chain	State
Company Five*	<500	Decorative & giftware	Private Ltd. company
Company Six*	500+	Industrial & consumer products based on polypropylene	Private Ltd. company

* The identity of these companies is confidential at the request of the companies.

The research was longitudinal in nature conducted in two phases during 1987. Initially, as much background information as possible was gathered about the companies from secondary sources such as annual reports, public domain commentary and any other sources of information. Secondly, interviews were conducted with the chief executives of the companies concerned. The interviews were structured around the following issues:

- Causes of decline as perceived by the (current) chief executive
- Previous strategies practised
- The turnaround process in general
- Examination of specific changes made within the company.

Discussion

Hofer developed a turnaround strategies performance model which compares recommended and actual turnaround strategies for companies and then indicates their success. The authors have applied this model to six companies in the sample of their research. The model assesses the company's operating and strategic health prior to the turnaround in order to indicate a turnaround strategy. Such strategies for the company are recommended by analysing the causes of decline for the company. Hofer applied this model to the twelve companies in his sample. He found that out of the six companies which succeeded in their turnaround that their actual strategy was consistent with the recommendations of the model.

The authors of this study also found a significant consistency with the model in the case of the six Irish companies. From the research data the problems of each company were analysed in operational and/or strategic terms. This indicated a suitable turnaround strategy to be pursued. Whether this strategy was in fact adopted was examined, as also were the subsequent performance results of each company. This enabled corroboration with the model (see Exhibit 2).

Exhibit 2

Turnaround Strategies Performance Model

Company	*Current Operating Health*	*Current Strategic Health*	*Indicated Turnaround Strategy*	*Indicated Strategy Adopted?*	*Performance Result Achieved*	*Corroboration with Model*
B & I	Very Weak	Average	Operating	No	Continued Losses	–
Bewleys Cafes	Weak	Very Weak	Operating/ Strategic	No/ Yes	Profits Anticipated	+
Arklow Pottery	Weak	Very Weak	Operating/ Strategic	No/ No	Continued Losses	–
Great Southern Hotels	Very Weak	Weak	Operating/ Strategic	Yes/ Yes	Profits	+
Company Five	Weak	Very Weak	Operating/ Strategic	Yes/ Yes	Profits	+
Company Six	Average	Weak	Strategic	Yes	Profits	+

It can be seen that this corroboration was, in broad terms, good. The experience of four out of the six companies was largely consistent with the model. Four of the companies were characterised by strategic and operational weakness, with the strategic situation being notably weak in three of them. Of the other two companies, it is significant that their more positive dimension was at best only average. Further studies might well confirm that many companies in need of turnaround from a base of chronic difficulty might well require attention to both dimensions.

The companies which followed strategies which were not recommended by the model experienced even further decline or did not improve their situation. Out of the six companies in the sample, five of the companies appointed a new managing director to carry out the turnaround. The only company which did not appoint a new managing director was Company Six and as this company did not experience any serious decline — the time criticality of the situation was not urgent — there was no need to make immediate changes at top level management. This result is consistent with all the literature on turnaround which says that management change is a pre-condition for a successful turnaround. Although Company Six did not appoint a new managing director, it did introduce a more professional management approach.

An important underlying condition in the turnaround strategy was financial backing. In the case of state companies, this did not appear a major problem, and in the case of the private sector companies successful negotiations with financial institutions were the first step in the turnaround process. While the research does not indicate examples where successful financial re-structurng was absent and consequently that the turnaround effort might have failed, this is an area that is worthy of further investigation. It should be noted that in Hofer's model fundamental preliminary financial re-structuring is not given the importance which seems to be required in most turnaround situations, even though some of his suggested strategies, such as sale of assets, do constitute an element in financial re-structuring. All of the companies except one emphasised the importance of strategic planning in the turnaround process, and it is interesting to note that this one company has been the least successful in its turnaround efforts.

Important issues arise concerning the role of strategic marketing in the context of turnaround strategy. Because of what might be considered the current fashion for marketing, marketing 'solutions' are often the automatic focus of remedy among those faced with turning around organisations in difficulty. And in particular, operational marketing 'solutions', such as increased advertising, are often implemented, because they are very readily available. Not alone may operational marketing remedies be the incorrect solution but strategic marketing change may also be inappropriate. Fundamental defects may more often exist in the financial structure of the organisation, in the production operating efficiency or in personnel management. On the other hand, where a company is dominated by a particular ethos such as production engineering or accounting, solutions may be sought solely in these areas because of the technical competence and background training of these personnel when in fact fundamental strategic marketing change is required. These comments may serve as a necessary caution against unidimensional solutions.

This article has focused on the theoretical body of knowledge that has developed in recent years in the area of turnaround. It has applied one particular model to companies in the Irish context requiring turnaround strategies and demonstrates the general usefulness of such a model in turnaround analysis, and the very positive degree of corroboration between model generated solutions and successful turnaround response. Some of the issues raised require further research and while the model used proved particularly appropriate to the study, more comprehensive models of analysis would be of value. Furthermore, the context in which marketing decision-making should operate in turnaround situations is identified and the limitations and possibilities of marketing's contribution are stressed.

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