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## Five Stages to Managing Successful Turnarounds

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The process of turning around a troubled entity is complex, due to multiple constituencies, usually including lenders, creditors, investors, owners and employees. All have different agendas. In my work I address the turnaround process as if all constituents are in favor of proceeding to the end, when a restructured entity emerges. Nothing about a turnaround is simple, but that approach at least clarifies the forward movement.

Above all, focus on the management team. Businesses fail because of mismanagement. According to a study conducted by the Association of Insolvency and Restructuring Advisors, only 9 percent of failures are due to influences beyond management's control. Mismanagement is most often seen in more than one of these multiple areas: autocratic style, ineffective personnel management, vague goals, lack of new customers, inadequate strategic analysis, and mismanaged growth.

So, as Will Rogers said, "If you find yourself in a hole, stop digging." Good advice for directors with responsibility to lead a company.

Turnaround specialists are often an excellent choice. They bring a new set of eyes, trained in managing and advising in troubled situations. These experts are either practitioners or consultants. Turnaround practitioners take management and decision-making control as the chief executive officer or chief restructuring officer.

Turnaround consultants on the other hand advise management, perhaps the same management that failed before.

The key is to build enterprises that future buyers want to invest in. That's what turnaround professionals do.

Here are the five major stages in the turnaround process:

### Stage 1: Management Change

It is important to select a CEO who can successfully lead the turnaround. This individual must have a proven track record and the ability to assemble a management team that can implement the strategies to turn the company around. This individual most often comes from outside the company and brings a special set of skills to deal with crisis and change. She will stabilize the situation, implement plans to transform the company, and then hire a replacement.

It is essential to eliminate obstructionists who may hamper the process. This could require replacing some or all of top management. This will undoubtedly mean also replacing some of the board members who did not keep a watchful eye.

### Stage 2: Situation Analysis

Your objective is to determine the severity of the situation. Is the business viable? Can it survive? Should it be saved? Are there sufficient cash resources to fuel the turnaround? This analysis should culminate in formulating a preliminary action plan that shows what is wrong, what potential solutions exist, key strategies to turn the entity in a positive direction, and a cash flow forecast (at least 13 weeks) to understand cash usage.

Important steps at this stage: Identify what product and business segments are most profitable, particularly at the gross margin level, and eliminate weak and nonperformers. Make certain that all functional areas (sales, production) are working to support the goals of their counterparts.

### Stage 3: Emergency Action

You have to gain control of the situation, particularly cash, and establish breakeven. Centralize cash management to ensure control. If you stop cash bleed, you enable the entity to survive. Time is your enemy. Protect asset value by demonstrating that the business is viable and in transition.

Usually you have to raise cash immediately. Review the balance sheet for internal sources of cash such as collecting accounts receivable, and renegotiating payments against accounts payable. Sell unprofitable business units, real estate, and unutilized assets. Secure asset-based loans if needed. Restructure debt to balance the amount of interest payments with a level a company can afford.

Lay off employees quickly and fairly. It is much better to cut deeply all at once, than to make small cuts repeatedly. Remaining employees can focus on work if they have (relative) job security.

### Stage 4: Business Restructuring

The goal is to create profitability through remaining operations. Stress product line pricing and profitability. Restructure the business for increased profitability and return on assets and investments. At this stage your focus should change from cash flow crisis to profitability. Fix the capital structure and renegotiate the long and short term debt.

Incentive-based management will drive employees to get involved smartly. Create teams of employees to identify and rework inefficiencies and promote profitability. There are only two ways to increase sales. Sell existing product to new customers. Sell new products to existing customers. Do both if you want growth.

#### Stage 5: Return to Normal

Now its time to institutionalize the changes in corporate culture to emphasize profitability, ROI, and return on assets employed. Seek opportunities for profitable growth. Build on competitive strengths. Improve customer service and relationships. Build continuous management and employee training and development programs to raise the caliber of your human capital.

This could be time to restructure long term-financing at more reasonable rates now that the company is stable and on a growth path.

The odds of success increase dramatically if a turnaround plan including these stages (see below) is implemented and followed.

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Turnaround Phases and Actions					
Stage	Management Change (Leadership)	Situation Analysis (Viability)	Emergency Action (Crisis Control)	Business Restructuring (Change)	Return to Normal (Going Concern)
<b>Objectives</b>	<ul style="list-style-type: none"> <li>Put top management team in place.</li> <li>Select turnaround specialist.</li> <li>Replace some/all top management.</li> <li>Eliminate impediments.</li> </ul>	<ul style="list-style-type: none"> <li>Can the company survive?</li> <li>Should it be saved?</li> <li>Is the business viable?</li> <li>Are cash resources available to fund turnaround?</li> <li>Develop preliminary action plan and nature of turnaround.</li> </ul>	<ul style="list-style-type: none"> <li>Go into survival mode.</li> <li>Get control.</li> <li>Establish breakeven.</li> <li>Turn cash flow positive.</li> <li>Raise cash to support turnaround.</li> <li>Protect resources.</li> <li>Protect asset value.</li> </ul>	<ul style="list-style-type: none"> <li>Create profitability through operations.</li> <li>Restructure business for increased return on assets and investment.</li> </ul>	<ul style="list-style-type: none"> <li>Seek profitable growth.</li> <li>Emphasize profits and returns.</li> <li>Build competitive strengths.</li> </ul>
<b>Sales and Marketing</b>	<ul style="list-style-type: none"> <li>Jump-start sales.</li> <li>Drive revenue.</li> <li>Volume in = revenue.</li> </ul>	<ul style="list-style-type: none"> <li>Analyze products and services distribution, sales and marketing strategies and systems.</li> </ul>	<ul style="list-style-type: none"> <li>Correct underpricing.</li> <li>Prune product lines.</li> <li>Weed out weak customers and distributors.</li> <li>Bring sales and marketing costs within industry average.</li> <li>Sell, sell, sell more.</li> </ul>	<ul style="list-style-type: none"> <li>Reassess competitive and product line pricing.</li> <li>Exploit existing products.</li> <li>Develop new products.</li> <li>Improve customer and distribution mix.</li> <li>Improve sales and marketing effectiveness.</li> </ul>	<ul style="list-style-type: none"> <li>Explore new markets and customer segments.</li> <li>Examine industry restructuring opportunities.</li> <li>Pursue value-added chain restructuring.</li> <li>Consider synergistic diversification.</li> </ul>
<b>Financial</b>	<ul style="list-style-type: none"> <li>Track cash.</li> <li>Develop trusted reporting and analysis.</li> </ul>	<ul style="list-style-type: none"> <li>Analyze cash flow, breakeven, profitability, cost reduction, balance sheet, and reporting gross margin by product.</li> </ul>	<ul style="list-style-type: none"> <li>Restructure debt.</li> <li>Improve working capital.</li> <li>Sell nonproducing assets.</li> <li>Reduce cost/increase revenue.</li> <li>Eliminate creative accounting practices.</li> </ul>	<ul style="list-style-type: none"> <li>Improve liquidity.</li> <li>Clean up balance sheet.</li> <li>Fix capital structure.</li> <li>Develop control systems.</li> <li>Create managerial accounting system.</li> </ul>	<ul style="list-style-type: none"> <li>Develop strategic accounting.</li> <li>Restructure long-term financing.</li> <li>Develop stock valuation and buyback system.</li> </ul>
<b>Manufacturing and Production Operations</b>	<ul style="list-style-type: none"> <li>Produce to meet sales levels only.</li> <li>Balance peaks and valleys.</li> <li>Volume out = throughput.</li> </ul>	<ul style="list-style-type: none"> <li>Analyze facilities, equipment, systems and procedures, and suppliers.</li> </ul>	<ul style="list-style-type: none"> <li>Shut down operations.</li> <li>Reduce work force.</li> <li>Reduce inventories.</li> <li>Control purchases.</li> <li>Increase productivity.</li> </ul>	<ul style="list-style-type: none"> <li>Develop productivity improvement programs.</li> <li>Re-evaluate overhead.</li> <li>Establish ongoing profit improvement programs.</li> </ul>	<ul style="list-style-type: none"> <li>Restructure operations for competitive advantage.</li> <li>Consider strategic alliances with world-class firms.</li> </ul>
<b>Engineering, Research and Development</b>	<ul style="list-style-type: none"> <li>Develop new products and services to support sales.</li> </ul>	<ul style="list-style-type: none"> <li>Analyze new product development, improvements in product, process, and productivity.</li> </ul>	<ul style="list-style-type: none"> <li>Accelerate high-potential projects.</li> <li>Shut down tangential projects.</li> <li>Unbundle product offerings.</li> </ul>	<ul style="list-style-type: none"> <li>Make new product market- and customer-oriented.</li> <li>Build an economic value-added orientation into process engineering.</li> </ul>	<ul style="list-style-type: none"> <li>Establish advanced technology monitoring systems.</li> <li>Seek competitive advantage, strategic leverage in all R&amp;D activities.</li> </ul>
<b>Organization</b>	<ul style="list-style-type: none"> <li>Organize for change.</li> <li>Rightsize the company.</li> </ul>	<ul style="list-style-type: none"> <li>Analyze systems.</li> <li>Does organizational structure make sense?</li> <li>Accounting/Control.</li> <li>Incentive/performance measurement and compensation.</li> </ul>	<ul style="list-style-type: none"> <li>Structure turnaround team.</li> <li>Review individual accountability and teamwork.</li> <li>Reward those who change the situation, release those who don't.</li> </ul>	<ul style="list-style-type: none"> <li>Restructure for competitive effectiveness.</li> <li>Develop rewards that reinforce turnaround.</li> <li>Demonstrate with action the seriousness of the situation.</li> </ul>	<ul style="list-style-type: none"> <li>Restructure to reflect changing strategies.</li> <li>Organize to succeed, then fill positions with talented people. Don't compromise.</li> </ul>
<b>Personnel and Human Resources</b>	<ul style="list-style-type: none"> <li>Hold employees accountable.</li> <li>Nurture critical human capital resources.</li> <li>Slow the turnover rate.</li> <li>Institute incentive-based management.</li> </ul>	<ul style="list-style-type: none"> <li>Analyze management team, sales, finance, and ops personnel, recruiting, selection, training, starting, and promotional systems.</li> </ul>	<ul style="list-style-type: none"> <li>Get peoples' attention.</li> <li>Establish who's in charge.</li> <li>Create a professional, business-like atmosphere.</li> <li>Sanction nonperformers.</li> </ul>	<ul style="list-style-type: none"> <li>Improve people mix.</li> <li>Institute incentive-based management.</li> <li>Bolster people to believe in consistent reward system.</li> <li>Get people to think profit, ROI, and cash flow.</li> </ul>	<ul style="list-style-type: none"> <li>Institutionalize continuous management and employee training and development programs.</li> <li>Grow human assets.</li> </ul>

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#### About the Author

John M. Collard is Chairman of Annapolis, Maryland-based Strategic Management Partners, Inc. (410-263-9100, [www.StrategicMgtPartners.com](http://www.StrategicMgtPartners.com)), a turnaround management firm specializing in interim executive CEO leadership, asset and investment recovery, corporate renewal governance, and investing in underperforming distressed troubled companies. He is a Certified Turnaround Professional, Certified International Turnaround Manager, Past Chairman of the Turnaround Management Association, serves on public and private boards of directors, is a frequent author, speaker, and advisor to companies, institutional and private equity investors, and governments. He was inducted into the Turnaround Management, Restructuring, Distressed Investing Industry Hall of Fame.

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