

# **Crisis Management, Recovery – Ways Out of Corporate Crises**

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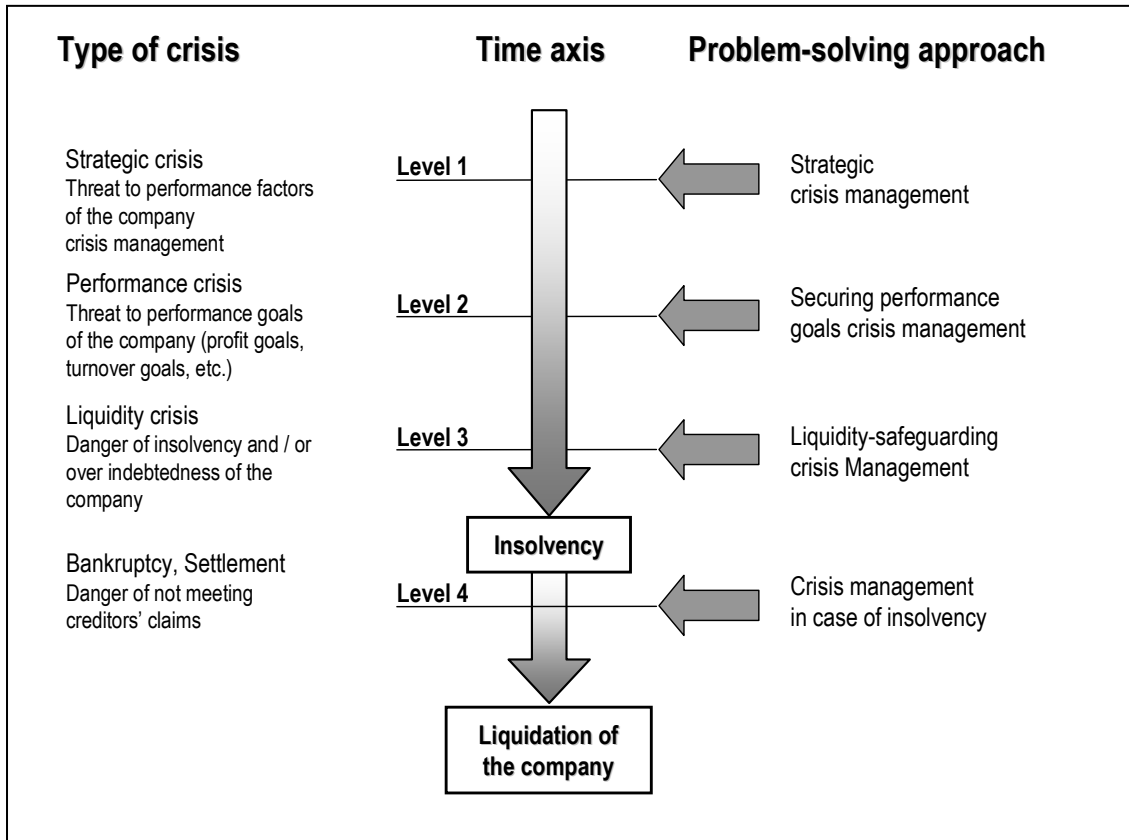
## 1. Causes and indications of corporate crisis

Every company must continuously readapt itself to changing market structures. This perpetual change is triggered by technological, ecological, societal and economic influences. The shift in values in society and increased environmental awareness also influence consumer habits and thus the demand for novel products and services. These challenges are first perceived by many companies more as threats than as opportunities for the future, as steps towards new fields of activity which the management must master with the use of various adjustment measures internally.

What are the indications that a company has missed the connection to developments in the environment, or even that it is already in a crisis situation? For the most part, it is primarily symptoms such as disorganisation, unnecessary internal quarrelling, high rate of fluctuation in leadership positions, defensive position of the management, missed opportunities in the market, poor working climate and last but not least, low staff motivation. If the situation has progressed that far, the moment for a timely reaction on the part of the management has often been missed. If the board of directors and the external institutions (such as banks, for example) do not analyse the desolate condition of their company in time, the only way out is: recovery. This is also the last moment in which the board of directors can obtain impartial support in seeking ways out of the corporate crisis by turning to an appropriate consulting firm which will set into motion and then guide the urgently necessary recovery.

## 2. Types of corporate crises

Corporate crises can be divided into four different types of manifestations. We adhere to the following model in our classification:



### Regarding Level 1:

*The company in a "strategic crisis".*

The performance factors of the company are threatened. The company leadership failed to adapt its strategic concept to the economic and structural market and environment conditions.

Problem-solving approach:

A new strategic corporate concept must be formulated. In general, it includes:

- a plan of procedure for withdrawal from the unprofitable business areas;
- a catalogue of measures for long-term improvement of the offer and the market processing;
- proposals for diversification, co-operation and acquisition measures in promising business areas.

**Regarding Level 2:**

*The company in a "performance crisis".*

The performance goals of the company (turnover, cash flow, contribution margins) have not been achieved.

Problem-solving approach:

Taking into account the new strategic concept formulated in Level 1, cost-cutting and turnover-effective steps are to be implemented, which will lead to the restoration of an adequate profit situation and secure it for the future.

**Regarding Level 3:**

*The company in a "liquidity crisis".*

The company cash flow is inadequate, perhaps a cash drain is drawing on liquid assets. The classic crisis situation.

Problem-solving approach:

Measures which eliminate the cash flow problem in the short term and improve the company's self-financing have first priority. Only afterwards are the tasks in Level 1 and 2 to be tackled.

**Regarding Level 4:**

*The company in an "insolvency crisis".*

The creditors' claims can no longer be satisfied completely. Insolvency and over indebtedness lead to default.

Rescue attempt:

Only if a recovery concept has a chance for success can the threatening bankruptcy be averted with a settlement. If this is not the case, this highest crisis level ends with the liquidation of the company.

### **3. Procedures in crisis handling**

In the following section, the phases of crisis handling will be described in more detail. It is to be assumed that the company in need of recovery is in a crisis of liquidity (Level 3: Liquidity crisis). The following measures are at the forefront in finding a solution to this situation:

#### 3.1 Preliminary clarification phase

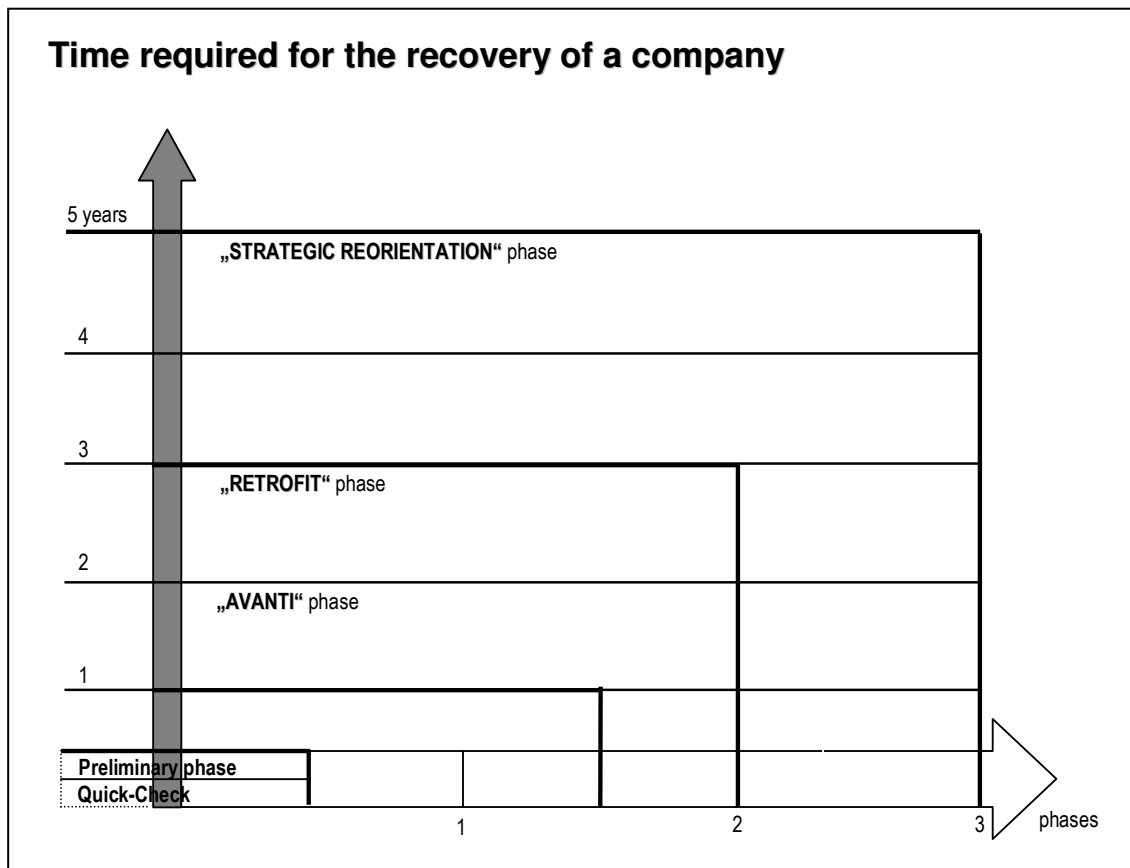
During a concentrated preliminary clarification phase, to be undertaken without delay, the following points are to be realised by the board of directors, any investors and the external consulting organisation:

- Carrying out of an immediate analysis, a "Quick Check", by the external consulting firm. Taking stock of the current status, examination of all possibilities and opportunities of the recovery measures.
- Joint establishment of measurable project objectives, drawing up of a plan for procedures and deadlines.
- Definition of the project organisation (board of directors/project team/working groups), as well as the role of advisor (crisis manager).

Assumption of temporary management functions on-site (crisis management) by the specialists from the consulting firm which has been engaged.

If the company is in an advanced crisis situation, a lengthy amount of time is usually necessary to bring it back to a state of prosperity. Unfortunately, this fact is usually underestimated by those involved. They believe that the company can be put back on its feet with a wave of a magic wand in the direction of costs. This type of crisis handling can quickly boomerang, because the basis for a lasting success has not been created. Short-term crisis management is only possible through the sale of a company. If this possibility is to be avoided, it is usually necessary to proceed through 3 levels (see following illustration) in order to have a successful corporate recovery.

The time necessary for the recovery of a company is generally between 1 and 3 years, but can last as many as 5. The individual recovery phases normally take place simultaneously. Only at the beginning of the crisis management does the main activity lie in the "AVANTI" programme. Here, the insurance of short-term survival is the intention.



### 3.2 „AVANTI“ phase

Should a company find itself in a position where its existence is threatened, such as a liquidity crisis, all forces must be mobilised without delay in order to insure its short-term survival. This calls for defensive behaviour in the first instance. Cost-cutting measures, liquidity-producing activities (such as stock reduction, special sales, etc.) take initial precedence. Short-term orientation towards results has absolute priority. The sources of loss, already investigated in the "Quick Check" (Level 1), must be eliminated. The following sample response characterises this situation:

*"AVANTI" package of possible immediate measures*

- *Lower fixed costs*
  - Reduce active and fixed investments
  - Relieve the liabilities side of the balance sheet
  - Lower overhead
  - Possible dismissal of personnel
  
- *Lower variable costs*
  - Material costs
  - Inventory and transportation costs
  - Energy costs
  - Marketing costs
  - Increase productivity

- *Increase profit*
  - Raise selling prices and quantities
  - Streamline product assortment (ABC analysis)
  - Stock reduction sales
  - Special sales/sales promotions
  
- *Secure liquidity*
  - Dialogue with banks/creditors/major suppliers
  - Short-term tide over loans
  - Possible moratorium
  
- *Secure company leadership*
  - Review leadership personnel/build new crew
  - Organisational adjustment (structure and processes)
  - Introduce new leadership rhythm
  - Create motivation/trust (in all target groups externally and internally)

Securing the company leadership creates special problems during this phase. The "replacement" of the previous company owner, for example, usually results in great disquiet among the personnel. It is important that those newly responsible for the leadership elaborate a problem-solving catalogue (the "AVANTI" programme) together with the remaining team and convert it immediately into activities. If leadership during this phase is quick, consistent and target-oriented, the first successes will begin to appear. When a trend reversal is in sight, a positive climate will soon be felt among the remaining personnel. As a result the 3rd phase, "RETROFIT", can then be introduced smoothly.

### 3.3 „RETROFIT“ phase

In contrast to the "AVANTI" activity package, which is oriented to the short term, the "RETROFIT" phase is when the basis for a new company future should be created. A reorientation of medium-term character is of primary importance. The greatest difficulties have been weathered thanks to the "AVANTI" programme. Now the specific recovery activities can be introduced in order to bring about a continuous recovery for the shaken company.

*Possible points of emphasis during the "RETROFIT" phase are:*

- *Readjusting the balance sheet*  
Bringing in new funds, execution of disinvestments not important to the company.
- *Reorganisation and restructuring*  
Including personnel redeployment and replacement
- *Setting up a leadership and information system*  
Internal report system, creation of yield and cost transparency.
- *Continuation of cost-cutting measures*  
Savings measures. Modernisation investments, value analysis, increase in efficiency.

- *Reformulating of the marketing policy*
  - Analysis of the needs of the sales partners
  - Reformulating of the offer policy (offering problem-solving to the customer)
  - Strengthening and differentiation of marketing communication
  - Extension of distribution
  
- *Strengthening the motivation of employees*
  - Wide communication of the corporate goals
  - Example-setting behaviour of the new management ("models")
  - Employee dialogue
  - Creating a new company philosophy
  
- *Systematic goodwill attention to all external groups (PR programme)*

The execution of the "RETROFIT" programme takes time - usually 1 to 2, many times up to 3 years! Once the restructuring is complete, the real crisis management or the recovery, in the strictest sense, also comes to an end. It would be cardinal mistake, on the other hand, to give up all the measures being taken towards corporate recovery at this point! For it is only now that the conditions exist within the company which will allow for dealing thoroughly with the long-term development possibilities.

#### 3.4 "Strategic reorientation" phase

Concurrently to the recovery measures effective in the short and medium term (the "AVANTI" and "RETROFIT" phases), dealing with the future of the company in recovery must also occur; that is, the strategic performance factors must be reformulated. The new company strategies are to be worked out by a strategy team (e.g., composed of members of the board of directors, employees in leadership and external consultants) in workshops which take place at regular intervals. Among other things, the long-term thrust within the individual business units, financing alternatives, emphasis in investments, and also possibilities for collaboration with third parties will be established. This phase concludes with the elaboration of detailed marketing plans, which normally takes approximately 6 months.

#### **4. Points of particular importance in crisis management**

*In the preliminary clarification phase: gloves-off, rough analysis ("Quick Check"), clear statement of tasks and comprehensive division of responsibilities in crisis management.*

Corporate crises appear in manifold forms. They can be traced to the most diverse causes. But one thing is common to all: They can only be overcome if the company management ruthlessly exposes the causes and the type of crisis through a comprehensive and precise analysis, and is capable of making rapid decisions. In short: If it is able to introduce professional crisis management and to carry it through in a consistent manner.

*The spiralling failure is to be halted as soon as possible and the trend reversal introduced with the use of all means at hand.*

A package of immediate measures (the "AVANTI" phase) aims at eliminating the major sources of loss and strengthening the financial basis. It is a question of setting the right examples in an intricate situation! Although personnel measures cannot generally be avoided, an overreaction must carefully be avoided, because the company-specific know-how belonging to the leadership is of eminent importance - provided that the leadership is motivated to commit its skills to the further service of the company.

*Avoid overreaction, mobilise positive forces, re-establish trust through visible successes.*

Within the "AVANTI" and "RETROFIT" phases, it is also important to mobilise the available positive forces through the use of signals. The recovery plan is to be converted into reality with targeted projects. It is a question of re-establishing trust with employees, customers, suppliers and banks through visible successes.

*In the crisis, do not react only defensively: go on the offensive as well!*

Crisis management is primarily defensive. Cost-cutting and saving measures are of primary importance. It is even more important - parallel to these immediate measures - to introduce and carry through offensive steps within the framework of a new corporate strategy. Even less spectacular offensive steps can serve greatly to motivate a staff during a crisis phase. Investments in modernisation or dealing with new markets have stimulating signal effects: Following a "shake-out" phase, they make it unmistakably clear that the company will carry on.

## **5. Possibilities for the external advisor in corporate recovery**

The leadership task which presents itself in overcoming an individual case for recovery is very complex. The affected management requires confidence, courage and honesty in handling the crisis. Without new deliberations on the part of the corporate leadership and the employees, without repressing earlier private interests, without a change in the existing entitlement mentality, the company will never be brought back afloat to steer clear of rocky reefs.

The intervention of an external corporate advisor represents an auspicious way out of the dilemma. He can approach the task at hand without prejudice, with distance (and without a "past"). Thanks to his expertise and experience, he is able to intervene immediately in the unhealthy operational process and set the company on a new course (catalyst effect). The company in crisis must be careful that the consulting firm it chooses has sound crisis know-how, broad knowledge, specialised expertise, and management experience at its disposal.

## **6. Summary**

In the life cycle of a company, critical phases alternate with longer-lasting periods of relative prosperity. By the time a company management has recognised and accepted a critical phase as such, it often happens that valuable time has been lost. The critical phase escalates into a crisis. The following, multi-stage procedure has proven itself in the handling of classic corporate crises:

- Preliminary clarification phase,
- "AVANTI" phase,
- „RETROFIT“ phase,
- "Strategic reorientation" phase

Following thorough and rapid preliminary clarifications, the most serious sources of loss are eliminated during the "AVANTI" phase in order to insure the liquidity and the short-term survival of the company. During the "RETROFIT" phase, the affected company must be revitalised in terms of performance, finances and organisation. Finally, the corporate performance factors are newly formulated and strengthened through a strategic reorientation. For the evolution of this complex task, the project organisation has proven its worth in practice. The collaboration of external advisors offers substantial advantages.

## The sequence of a crisis management in key words

(Represents a company which finds itself in a crisis of liquidity.)

### *Preliminary clarification phase*

- Establish task and goal-setting of crisis management
- "Quick Check" (taking stock of status, gloves-off rough analysis) by external consulting firm
- Establishing the project organisation
- Conveying individual project phases, setting up deadline plan
- Deployment of crisis management.

### *„AVANTI“ phase*

- Continue problem analysis through interviews and enquiries
- Elaboration of "AVANTI" programme catalogue of immediate measures with the new leadership crew
- Providing information to personnel and other target groups
- Carrying out of "AVANTI" measures such as
  - Lowering costs
  - Increasing profits
  - Securing liquidity
  - Improving company leadership.

### *„RETROFIT“ phase*

- Readjusting the balance sheet
- Reorganisation/restructuring
- Setting up a new leadership and information system
- Continuation of cost-cutting measures
- Reformulating of the marketing policy
- Realisation of modernisation investments
- Strengthening the motivation of employees
- PR programme for goodwill attention to all target groups.

### *"Strategic reorientation" phase".*

- Company analysis/analysis of environment/market analysis
- Development of new corporate strategies (guiding principles / performance factors / product-market priorities / operational emphasis)
- Strategy implementation.

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