

The strategic leader

Successful turnarounds: three key dimensions

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"There is nothing more difficult to take in hand, more perilous to conduct, or more uncertain in its success, than to take the lead in the introduction of a new order of things" (Niccolo Machiavelli, *The Prince*).

If your company needs a massive transformation to survive, then a one-sided response – across-the-board-layoffs or a new tranche of funding – is unlikely to set the stage for sustainable results. According to our research and experience, successful corporate turnarounds require a response that addresses three dimensions of an organization's problems. They require an overhaul of finances, of strategy, and of corporate pride. Moreover, true turnaround artists attack these dimensions simultaneously and with a high-speed process.

The most successful turnarounds, in fact, according to a Bain & Company study of 21 top-performing business transformations of the past decade, happen within 20 months. Key managerial changes were made at the outset. To transform finances and strategy, these turnarounds focused on results, not elaborate change practices. To reinvigorate company pride, CEOs reached out through speeches, events and targeted incentives to re-energize employees and executives. Indeed, among the 21 companies Bain studied, all of which took that approach, stock prices rose on average 250 percent during and after the turnaround

process (for some companies, the rise was more than 1,000 percent per year). The top five performers' annual stock appreciation exceeded 250 percent.

Where to start?

Financial turnaround: Shoring up your balance sheet and cash position is the first order of business in corporate turnarounds. Once that picture is clear, then managers can set realistic budget goals and measures that will tell whether the organization is on track from day-to-day, and week-to-week.

Consider Optus Communications, a 1992 start-up and the number two telecommunications firm in Australia. After a promising start, by the mid-1990s the company faced a host of problems, including the end of Australia's telephone duopoly, a cash-hemorrhaging subsidiary, a repeatedly-delayed IPO, and a revolving-door CEO's office. In 1996 these problems culminated in a staggering before-tax loss of \$667 million. In June of 1997, shareholders came "within an inch of liquidating the company[1]".

But instead of a line gone dead, investors soon heard the clear tone of a profitable company. First, Optus' CEO was fired and an entirely new management team installed. A problematic subsidiary, Optus Vision, was integrated, and its cash outflow brought under control. Project

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Breakeven, targeting a variety of short-term opportunities, yielded \$260 million in pretax earning improvements. Optus' balance sheet underwent a complete reworking. By quickly appointing the talent to tackle finances and bring the balance sheet back to health, Optus freed up other executives to focus on strategy and incite the ranks. An employee stock ownership plan was put in place, and senior management team objectives and incentives were completely restructured. Finally, the long-delayed IPO was successfully launched. Elapsed time – one year.

By 2001, Optus had turned in four consecutive years of profitability and was among the top ten Australian companies in market capitalization. In September of that year, Singapore Telecom acquired Optus for more than double the IPO price, locking in more than \$9 billion in shareholder value created since the turnaround began. After a challenging transition, Optus has continued to defy the market with strong, double-digit growth, and is considered the jewel in SingTel's crown.

Strategic turnaround: Faced with trouble, many senior leaders behave as though their companies can “reset” themselves simply by doing the same things – rallying around the same goals – with fewer people. Not so. Successful turnaround stories – turnarounds with sustainability – usually involved substantial strategic repositioning.

It's important to emphasize that even the savviest strategy can't succeed without ability. And that means a strong management team. Nearly all successful turnarounds replace senior management who cannot perform up to the company's new standards, or who fail to commit to the organization's new direction. Bain's research shows that replacing senior management correlates closely with successful change, but broad employee layoffs do not. Almost every one of the 21 textbook turnarounds substantially replaced the senior team. At Optus, 14 out of 15 top executives were replaced. At Continental Airlines, a well-

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documented turnaround success of the late 1990s, 50 of 61 senior executives were let go in the early months of the company's transformation, with only about 20 new faces replacing them. And at European publisher Reed Elsevier, CEO Crispin Davis replaced 11 out of 12 top executives in 1999 during a turnaround that lasted just under two years and turned Reed from an under performing and strife-ridden company into a stock-market hero. “It was clear that management had to be wrong if a company like this was performing that poorly”, said Davis. Making such personnel changes can be extremely painful for the entire organization. Often, top managers find themselves in the difficult position of having to jettison close, personal friends. But as the research demonstrates, this extremely difficult step is also one of the most meaningful in turning a company around.

Pride turnaround: Third, the most successful turnarounds pay close attention to employee morale as they move towards renewal. Faced with massive change all around them, employees are naturally going to show resistance, even if it is involuntary, to the

process. In companies restructuring and transforming to stave off bankruptcy – like Kmart or Polaroid recently – employees usually suffer lowered self-esteem. In either case, top leadership must lead the charge to reclaim collective pride.

Kevin Ryan, CEO of contact lens maker Wesley Jessen, says you have to restore trust, dignity, and drive to company culture. You start by making it a place where people want to come to work again. You practice and require honesty at all levels. And you communicate a simple, powerful set of messages to employees. Then you communicate those messages again.

Ryan knows whence he speaks. Wesley Jessen, a loss-making division of health-conglomerate Schering-Plough, was spun off in a management buyout in June 1995 with survival looking touch and go. Ryan and his team quickly tackled financial and strategic turnarounds – redeploying assets and refocusing the business on specialty contact lenses. This took the company out of head-to-head competition in the mass market with lens titans Johnson & Johnson and Bausch & Lomb.

Three sides of an effective turnaround

Financial side:

- Stabilize cash flow; and
- Shore up the balance sheet.

Strategic side:

- Develop a clear and cogent strategy;
- Communicate its principle;
- Replace managers who cannot deliver; and
- Do not “automatically” pursue broad employee layoffs and avoid repeated downsizing.

Pride side:

- Restore trust, dignity, and drive to company culture;
- Tell employees what the key success factors are and celebrate achievements; and
- Acknowledge the innovative employees and the high performers and eliminate the drones.

Yet observers point to CEO Ryan's ability to crank up the voltage for his employees as a big part of returning the company to 20/20 vision. Achieving this required Ryan's considerable charisma and communication skills. "You are here", he would say to employees time and time again, from senior management down to the factory floor, "because you want to be". The message: those who didn't believe that the company could be saved were free to leave. Those who remained would do so because they believed the prospects were enormous if everyone worked together.

At the same time that Ryan was over-communicating a very concise set of messages to the employees that remained. "You have to communicate really, really simply", he says. "People are going through a very traumatic event. Don't be cute about it. We had four statements, seven words. They were: 'Build volume. Spend effectively. Be accountable. Cash'. This is what we all have to do. Simple".

Ryan and his team built initiatives around each of the statements and communicated those in more detail to relevant managers. But in terms of transmitting the vision for success to the broader employee base, their communications were concise, simple, and hammered home again and again.

Ryan and his team took many steps to create an environment where people

would once again want to work. They shared successes: a "victory board" by the cafeteria celebrated new ad campaigns, sales achievements, and pictures of Hollywood movie stars wearing Wesley Jessen contacts lenses in their movies. They raffled off a Saturn automobile every six months, with raffle "chits" accumulating only if an employee had a perfect month's attendance ("That solved our direct labor attendance problem pretty quickly", notes Ryan). An informal "kangaroo court" also sprang up, with peers fining peers nominal sums for their more egregious mistakes, all done in good fun, and the proceeds went to a local charity.

Even more important than the fun, says Ryan, was the "ELM Principle" that he instituted when he took over the CEO job. ELM stands for ethical, legal, and moral, and these became the guiding principles of the company. Implicit in them was a complete honesty and openness with and among employees, even about the bad news. Leading by example, Ryan let people know when cost-cutting or lay-offs were happening, and why. He also made a point of sharing the company's financial results with employees on a monthly basis. This was something that previous management had not done and that Ryan didn't have to do (the company was privately held). As it turned out, this policy quickly became a morale booster: from a run rate of a \$40 million

annual loss, the company turned a profit in its first month under Ryan's stewardship, and had a consistent track record of quarterly profitability until CIBA Vision acquired it in October of 2000.

In 1997 the company issued a successful IPO, garnering a market cap of \$290 million (a 45x return). Then in May 2000, the company agreed to be acquired by Novartis AG's CIBA Vision Corp. for \$785 million, another 2.7 times appreciation in equity. The company is now the world's largest maker of specialty contact lenses.

Fast, focused, simultaneous and thorough

Successful turnarounds come to companies of all sizes and shapes. Bain's study included large companies and small, public and private, diversified and focused, and regional and international, from a variety of industries. The challenges those companies faced ranged from survival to slowing growth to business redefinition. What these companies had in common was avoidance of the biggest turnaround pitfall: failure to move far enough, fast enough, or thoroughly enough to save their businesses.

Note

1. *Australian Financial Review*, 4 July 1997.