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Turnaround Management in South-East Asia
- Research Challenges -

By

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Abstract

Research on turnaround management for a Western environment has over the past decades developed meaningful insights into the turnaround process and turnaround strategy content. Many of the Western findings were assumed to be generalizable across business settings and environments.

The experiences during the Asian crisis, however, changed the understanding of the appropriateness of Western turnaround recipes for South-East Asia: In the pre-crisis environment, many Western investors held stakes in South-East Asian companies. As the Asian crisis severely hit the financial basis of many Asian firms and placed them in turnaround situations, the Western investors recommended Western turnaround concepts. Neither the underlying turnaround process models nor the recommended turnaround strategy content, however, were particularly successful in the South-East Asian environment. The experiences of the Asian crisis, therefore, indicate an inappropriateness of Western turnaround concepts in South-East Asia and a substantial gap in the turnaround literature.

After contrasting turnaround with related concepts and placing turnaround management in the frame of strategic management, the turnaround literature is reviewed focusing on turnaround process and turnaround strategy content in the Western environment. After analyzing the turnaround literature for a Western environment, research on turnaround in South-East Asia is presented highlighting the conceptual and analytical differences.

Idiosyncrasies in the South-East Asian turnaround process include the recognition of decline, the ability to retrench, CEO replacement, speed of turnaround and matching of turnaround cause and response. Turnaround strategy content in the Western environment is retrenchment oriented. Since, however, retrenchment cannot be implemented in South-East Asia as rigorously as in the Western environment, the strategy content in South-East Asia is different from Western strategy content.

I argue that due to the differences in the turnaround process and the turnaround strategy content between the Western and the South-East Asian environment, these two research areas are fruitful fields for future research attention.

Keywords: Turnaround Management, Turnaround Process, Turnaround Strategy Content, South-East Asia

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1. Introduction

In the early 1990s, massive equity and debt investments poured from Western countries into South-East Asia. Particularly, geographically diversified, global or international Western firms further extended their business portfolios to South-East Asian countries in the pursuit of leveraging or complementing their business models. Many of the equity engagements of Western companies were undertaken as joint ventures. Similarly, investments made by financial investors were commenced as transfers of funds to South-East Asia in exchange for equity holdings or debt titles.

In 1997 the Asian financial crisis abruptly changed the economic outlook of the Asian region. Starting with the severe devaluation of the Thai Bath on July 1st, 1997, a cascade of events effected currency valuations across Asia. The resulting economic downturn severely hit the financial basis of many companies operating in Asia.
As the dust of the Asian crisis has settled, many South-East Asian firms are faced with the challenge to recover from stiff performance declines.
Faced with performance decline in the firms in which they hold a stake, many Western investors and globally or internationally acting company leaders suggest their Asian counterparts to employ turnaround strategies proven successful in the Western hemisphere. It is, however, becoming increasingly apparent, that Western turnaround concepts are inappropriate in South-East Asia given cultural, legal and socio-economic differences.

In order for research on turnaround in South-East Asia to advance, the scientific knowledge and the missing elements of research on turnaround are reviewed in this contribution. The review is organized as follows: Firstly, turnaround is defined, contrasted with similar concepts and put ,in the context of strategic management. Thereafter, the Western model of turnaround is reviewed along the process and content dimensions to anchor the discussion of differences in South-East Asia. Based on the initial differences found in the literature, research gaps are identified.

1.1 Defining Corporate Turnaround

The concept of *turnaround* is broadly defined as the reversal of a declining situation, which is characterized by a negative performance trend and negative performance levels. Turnaround management correspondingly refers to the (management) actions taken to overcome a negative performance trend leading back to acceptable performance levels.

The broad definition of turnaround does not require the turnaround situation to be severe enough to endanger the survival of the company (as assumed by e.g. Hofer, 1980; Slatter, 1984; Barker and Mone 1994), but nevertheless *can* incorporate such a condition (Goodman, 1982; Robbins and Pearce, 1992; Pearce and Robbins, 1994).

Authors assuming corporate survival threats in turnaround situations argue, that situations of stagnating performance differ largely from turnaround situations, since a survival endangering crisis atmosphere creates more pressure on the top management to take certain measures (Grinyer, Mayes and McKiernan, 1988). Additionally, the assumption that the turnaround situation needs to be severe enough to jeopardize company survival can induce differences in outcomes of empirical studies (cf. Robbins and Pearce, 1992; Barker and Mone 1994; Pearce and Robbins, 1994). Since, however, a survival-threatening situation will usually time-sequentially follow a period of decline in which firm survival is not at risk, a broad definition of turnaround management allows for understanding the dynamics in the turnaround process more thoroughly (Arogyaswamy, Barker and Yasai-Ardekani, 1995).

Turnaround has been scientifically modeled from two distinct perspectives in the literature: On the one hand, organizational theorists around Starbuck and Hedberg have framed the turnaround situation from an *organizational behavior perspective* as organizational adaptation to environmental forces focusing especially on the deterioration of decision-making processes within organizations (Hedberg, Nystrom and Starbuck, 1976; Starbuck and Hedberg, 1977; Starbuck, Greve and Hedberg, 1978).

At the same time, based on case studies and longitudinal, large sample studies, a second group of researchers around Hofer and Schendel modeled turnaround as a strategic

decision-making problem. They assume that a turnaround situation can be cured by an appropriate turnaround strategy (Schendel and Patton, 1976; Schendel, Patton and Riggs, 1976; Hofer, 1980).
Most of the subsequent research on turnaround up to the present day has focused on the strategic management perspective. Arogyaswamy, Barker and Yasai-Ardekani (1995) reconciled the stagnation literature with the strategic management approach.

Since the concept of *restructuring* is sometimes used interchangeably with the turnaround concept, differences and similarities between turnaround and restructuring are briefly highlighted: Restructuring refers to the necessary changes for the firm – on the financial, portfolio or organizational level (Bowman and Singh, 1993) – to stay aligned with environmental conditions both internally and externally to thereby increase performance (Bowman et al., 1999). Financial restructuring refers to issues such as relations with the capital market, governance structures, leverage structures and associations with stakeholders (Bowman and Singh, 1993). Portfolio restructuring depicts changes in the scope of business engagements, e.g. through divestures or acquisitions, and organizational restructuring portrays changes in organizational structures and processes (Singh, 1993). Particularly financial- and portfolio restructuring provide ways to acquire financial resources by sales of parts of the firm or through changes in the leverage structure (Goldston, 1992).
Restructuring does not require a corporate crisis or a downward trend in performance, but might incorporate this condition. In fact, predominantly healthy companies commence restructuring initiatives to achieve envisioned configurations in alignment with anticipated future requirements of the environment.
Comparing corporate turnaround and restructuring, the following differences and overlaps becomes apparent: Turnaround refers to the process of overcoming a negative trend in company performance. Since a deficiency of corporate restructuring might result in a significant misalignment of the firm with its environment and therefore might lead to performance decline and eventually to a corporate crisis, a lack of restructuring can precede a turnaround situation. At the same time, restructuring measures of financial,

portfolio and organizational reformation might prove viable strategies in a turnaround situation. Particularly the acquisition of financial resources through financial and portfolio restructuring can be part of a viable turnaround strategy (Goldston, 1992). Since such restructuring actions can supplement or substitute other turnaround measures, the concepts of restructuring and turnaround overlap.

1.2 Strategic Management and Turnaround Management

A strategic management perspective is taken in most turnaround studies assuming that the turnaround situation can be cured by an appropriate turnaround strategy. This perspective emphasizes the implemented strategy in a troubled company over the process of how the strategy diffuses through the organization. However, organizational behavior aspects are relevant as far as they influence strategic decisions (Arogyaswamy, Barker and Yasai-Ardekani, 1995).

Since a strategic management perspective is taken in most turnaround studies, an introduction to the general field of strategy is provided to place the discussion on turnaround in the broader area of strategic management and to provide a structuring frame.

The concept of strategy is etymologically derived from the Greek words "stratos" meaning 'armed forces' and "agein" meaning 'to lead' originally referring to military concepts. Strategy in a business setting can be defined as a broad framework of instructions and guidelines for the tactical and operational running of a company often including explicitly formulated planning goals (Ulrich, 1990).

Ansoff (1965) first introduced the concept of strategic management. Strategic management extended the at-the-time widely accepted concept of strategic planning by an internal capabilities management.

The academic field of strategic management can broadly be divided into the area of *strategy process* (see e.g. Andrews, 1971; van de Ven, 1992) and *strategy content* (see e.g. Porter, 1980; Wernerfelt, 1984) both taking into account a certain context.

Strategy process can be defined from different perspectives including 'a logical chain of actions explaining causal relations between inputs and outputs', 'a category of constructs explaining actions' and 'a sequence of events and activities describing organizational changes over time' (van de Ven, 1992).

In the classical model, the strategy process is divided into the "strategy formulation" phase dealing with the decision-making process and the "strategy implementation" phase concerned with transferring decisions into corporate actions (Andrews, 1971). Due to criticism of the assumptions that the classical model makes, alternative process models have been developed (cf. Pettigrew, 1977, Mintzberg and Lampel, 1999).

In the area of strategy process, issues such as top management team composition (Hambrick and Mason, 1984), strategic change (Burgelman, 1991), organizational learning (Zahra and George, 2002), cognitive aspects (Narayanan and Kemmerer, 2001) and strategic decision-making (Eisenhardt and Zbaracki, 1992) are investigated.

The field of *strategy content* can be divided into the *market-based view* deriving generic strategies for the firm from the external competitive environment following the structure-conduct-performance paradigm (Porter, 1980) and the *dynamic capabilities approach* (Volberda, 1996; Teece, Pisano and Shuen, 1997) as an extension of the *resource-based view* (Wernerfelt, 1984; Prahalad and Hamel, 1990; Grant, 1991; Peteraf, 1993; Barney, 1996) both looking at internal resources and capabilities and the potential for leverage in the competitive environment.

The *market-based view* can further be differentiated firstly in the *Portfolio Theory* as an extension of the financial portfolio theory (Markowitz, 1952) to a business setting that found its main applications during the diversification era of the 1970s, and secondly in the *Positioning School* (Mintzberg, 1990).

The *Positioning School* has been in many ways the dominant paradigm in the field of strategy in the 1980s and continues to have considerable influence today. The focus of the analysis is the external competitive environment, the market conditions and the potential for monopoly rent creation by the firm through positioning relative to its competition. Following the structure-conduct-performance paradigm, the Positioning School assumes, that the profitability of a firm, measured as the surplus return over the cost of capital, is mainly determined by the structure of the industry or the structure of the strategic group the firm competes in, and is thereby rooted in the industrial organization economics. The units of analysis are industries, firms and products (Teece, Pisano and Shuen, 1997). The managers are modeled as rational decision-makers judging solely on a techno-economic basis. In that sense, the strategies creating competitive advantages result from the configuration of the environment, are generic in nature and can prescriptively be derived (Porter, 1980).

Especially since the 1990s, the internal perspectives offered by the *resource-based view* complements the external perspective of the Positioning School (Wernerfelt, 1995). In the resource-based view, the firm is modeled as a unique bundle of heterogeneous resources and capabilities. Organizational capabilities – interchangeably called competencies – refer to the capacity of the firm to undertake certain actions (Prahalad and Hamel, 1992). Interactions of intangible, tangible and human resources of the firm produce capabilities, which are the basis for a corporate strategy and result in competitive advantages depending on the key success factors in the industry (Grant, 1998). The role of strategic management is to lead the perception, exploitation and creation of resources and capabilities to achieve competitive advantages.

The idea of the resource-based view was expanded due to the hypercompetition firms encountered in the late 1990s (D'Aveni and Gunther, 1994). The *dynamic-capability approach* shifts the focus to the organizational capacity to renew capabilities for a dynamic alignment with changes in the environment and the creation and exploitation of dynamic capabilities through strategic management (Teece, Pisano and Shuen, 1997).

Dynamic capabilities are building on organizational resources and are exploited through organizational routines and processes. Dynamic capabilities are idiosyncratic in their particulars and dependent on prior actions in their materialization, at the same time being similar to the traditional formation of routines (sometimes combined with resources), which makes them less firm-specific on an abstract level than usually understood (Eisenhardt and Martin, 2000). Examples of dynamic capabilities include product development and strategic decision-making routines. The units of analysis are processes, positions and paths (Teece, Pisano and Shuen, 1997).

The market-based view and the resource-based view are complementary and ambivalent. Both perspectives look at deriving superior profitability: the market-based view identifies an attractive location within an industry gaining an advantage over rivals and the resource-based view identifies competitive advantages through superior resources or the superior leverage and exploitation of firm resources. In that sense, the prescriptions from the market-based perspective aim at the creation of monopoly rents whereas the prescriptions of the resource-based view aim at the creation of Ricardian or scarcity rents[1] and the capabilities approach at Schumpeterian rents. Since both concepts are closely linked and interdependent, the differentiation of the rent-creating source is difficult. In sum, monopoly rents, Ricardian rents and Schumpeterian rents compose the profitability of a firm, which is the ultimate measure of strategy performance.

2. A Western Model of Turnaround

2.1 Turnaround Strategy Process

This section presents four turnaround process models. The discussion of the four individual models highlights the main steps of the development of the turnaround process literature for a Western – mainly US oriented – cultural setting.

[1] Rents associated with the possession of superior resources, i.e. the rents above the costs of bringing the resources into production.

2.1.1 Early Perspectives on the Turnaround Process

In an exploratory study, Bibeault (1982) modeled the turnaround process based on descriptive statistics derived from a survey of 81 companies and over 100 interviews conducted with business leaders involved in corporate turnarounds. The analysis assumes conglomerate type organizations that can partly achieve turnaround through restructuring their portfolio of businesses.

Whereas the first two phases of the proposed turnaround process are predominantly concerned with the problem recognition, the phases three to five are action phases (see figure 1). The time frame for the different stages varies.
The turnaround process developed by Bibeault (1982) was initiated as a reaction to internal and/or external causes of decline. Internal causes are considered controllable within the firm and are usually the result of inappropriate management. In contrast, uncontrollable external causes can be politic or economic in nature, and might impose constraints on management actions.

In the *management change stage*, the top management realizes the performance decline and decides to react accordingly. Since Bibeault (1982) finds, that in seventy percent of turnaround situations, mismanagement is the reason for performance decline, under-performing members of the top management team are regularly replaced in the management change stage. The replacement of top managers is compulsory if they are either directly responsible for the mismanagement or if they are assumed to be unable to take necessary internal actions to achieve firm turnaround. As the responsible leader, the CEO is replaced especially if internal reasons are perceived to be the cause for the performance decline.

With effective management in place, the company enters the *evaluation stage*. In the evaluation stage, the viability of the company is assessed and a turnaround plan is developed that aims primarily at ensuring firm survival through liquidity management. To develop a turnaround plan, the top management has to gain sufficient understanding of the turnaround situation, the turnaround cause and organizational conditions to determine where the highest leverage of efforts can be expected in the short run. The turnaround plan, consequently, is based on the top management team prioritization of turnaround measures.

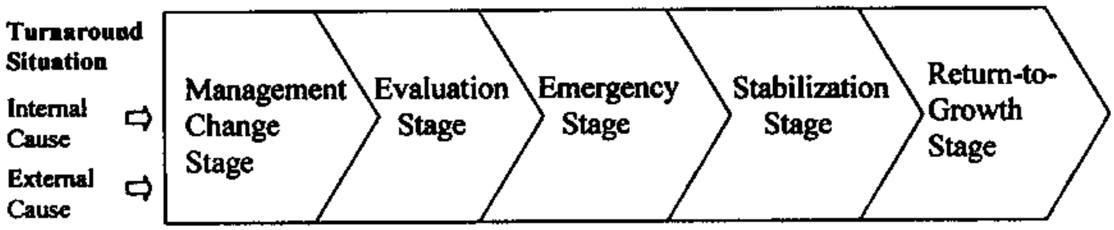

Figure 1: Early Model of the Turnaround Process
Source: Author's Depiction based on Bibeault (1982)

In the *emergency stage* the focus shifts from problem recognition to action. The most important goal at this stage is to ensure firm survival by focusing on liquidity. Retrenchment of assets and costs is the clear focus, as retrenchment is a short-term activity to increase liquidity by reducing cash outflow assuming a fixed level of cash inflow. Firm management, therefore, has to 'stop the bleeding' (Bibeault, 1982:99) by cutting costs. Actions taken to reduce cash outflows include personnel lay-offs and plant or department closings. Two assumption underlie the retrenchment activities: Firstly, personnel is seen as a cost factor rather than a source of competency. Secondly, the short-term focus on liquidity is governing the considered actions. Thereby, the long-term recovery strategy is neglected for a focus on short-term liquidity assuming an inability to increase cash inflow in the short-term.

Depending on availability of time and monetary resources, retrenchment activities might be more or less extensive. Accordingly, the emergency stage may or may not be a hurtful experience for the organization. If enough time is available in the emergency phase, the firm should try to divest plants and unprofitable business units through sales to strategic or financial buyers. Only if it is impossible to timely find a potential acquirer, the closing of parts of the business and disintegration of resources is unavoidable for short-term liquidity considerations. Overall, Bibeault (1982) strongly argues for the positive impact of retrenchment concluding, "it's also generally best to cut a bit too much, rather than too little" (Bibeault, 1982:100).

The retrenchment in the emergency phase, leads the firm to concentrate on business segments that achieve good profits or segments with promising gross margins. As a result of asset and cost-cutting moves, many organizations come out of the emergency stage with reduced revenue capacities and diminished resources, but with stabilized liquidity and more focused on core business.

With the elimination of negative cash flows, the firm enters the *stabilization phase*. In the stabilization stage, the strategic orientation shifts from short-term survival, retrenchment and liquidity management to long-term sustainability, acceptable return-on-investment

If the firm survives the emergency stage through retrenchment, and manages the stabilization phase with controlled profit growth without takeover bids or sales, it enters the *return-to-growth stage*. In this phase, the emphasis is on internal and external development and growth.

Internal development concentrates on revenue growth, new marketing initiatives, new ways to broaden the base of the existing business, and options to increase the market penetration.

External growth can potentially be achieved through an acquisition in the core business segment financed through funds from disinvestments. In order to achieve corporate growth, new products may be added; new markets penetrated and developed, selling effectiveness increased and customer services improved.

The executives put in charge in the management replacement stage might have led the company through traumatic retrenchment experiences, and as a result they might not be suited to lead the company in the return-to-growth stage since they might be incapable of creating a positive internal atmosphere. In such cases, Bibeault (1982) suggests a re-replacement of the turnaround management for long-term growth of the company.

The turnaround process ends if the perception of the company leaders is that the company has been turned around.

Many of the process elements that Bibeault (1982) proposes are the mirror of the 1970s and the conglomerate-type organizations that he analyzes. In the late 1970s many corporations traded at conglomerate-discounts due to mismanagement of their respective business portfolios. The turnaround process correspondingly suggests ways to refocus the conglomerate type organizations on its core business. Reviewing the companies that Bibeault (1982) analyzed unveils large organizations such as Electronic Associates, Amcord, and Johnson & Johnson and underlines the notion that this turnaround process is particularly oriented at the business setup of large conglomerates.

Nevertheless, Bibeault (1982) points out important restructuring options in a turnaround situation: These options include the exit from the current industry trough a sale or merger with a competitor, the potential to realize growth (and market share) in the core segments through acquisitions, and the ability for the turnaround firm to acquire financial resources through divestment of business divisions. The point is also clearly made, that divesting a business is clearly preferable over retrenchment of the business, since the divestment allows the firm to realize financial resources rather than building up obligations from the retrenchment process and disintegrating resources. Although the liquidity argument prevails, the notion of restructuring options is highlighted.

Much of the retrenchment and strategic renewal debate in contemporary turnaround literature is grounded in Bibeault's (1982) liquidity argument and the assertion that retrenchment is an integral part in the turnaround process. However, Bibeault (1982) does neither explicitly consider the negative effects of retrenchment nor assesses interdependencies between the early liquidity driven phases of the turnaround process and the later value and growth driven phases.

2.1.2 Contingency View

In a conceptual contribution, Hambrick (1985) assesses the stages of a successful turnaround attempt incorporating resource-oriented contingencies in the process model. The unit of analysis is the strategic business unit.

Hambrick (1985) argues that a turnaround situation is different from other strategic situations due to the limited available resources, poor internal moral, skeptical stakeholders and urgency. Since these contingencies are special to turnaround situations and particularly influence all stages of the turnaround, they are reviewed in more detail.

A low level of (financial) resources for Hambrick (1985) is by definition part of the turnaround situation. Depending on the length of time that the performance decline persists, increasing debt or overextending payable levels can provide short-term relief. However, banks are usually reluctant to infuse more funds in a declining firm. Consequently, one of the major challenges for the turnaround manager is to work with and stretch the available limited resources to achieve firm turnaround.

In addition to limited resources, the turnaround manager is confronted with *low internal moral* and dissatisfied personnel, which are consequences of the initial decline. With an increasing crisis situation a growing number of highly skilled and educated employees leaves the firm to work in a more stable environment. In a downward spiral poor morale, internal strife among personnel, and lack of confidence among employees further deteriorate the organizational resources and competencies (cf. Hambrick and D'Aveni, 1988).

Organizations depend on interrelations with *stakeholders* such as suppliers, creditors, distributors, franchisees, and unions since in times of performance decline the survival of the firm is partly dependent on the support of stakeholders and their confidence in firm survival. If firms suffer from declining performance, stakeholders withdraw their aid especially if they have better and more viable alternatives. The withdrawal of stakeholder support increases transaction costs for the firm (e.g. suppliers withdraw credit lines, banks/ bond-holder increase required interest rates) and further deteriorates resources, which increase the severity of the turnaround situation. The turnaround process according to Hambrick (1985), consequently, needs to incorporate stakeholder relationship management to avoid withdrawal of stakeholder support and to manage the expectations of stakeholders.

For Hambrick (1985) *urgency* is the result of the lack of time in the turnaround situation due to the low (financial) resource base, deteriorated internal moral and decreased stakeholder support. Accordingly, timely actions and fast decisions are crucial to firm survival. Moreover, urgency has implications for the way in which strategic decisions are made, the substance of those decisions and the sequence of actions.

The turnaround process consists of three action phases (see figure 2): In the *crisis phase* Hambrick (1985) assumes a firm survival-threatening situation. Correspondingly, the focus in the crisis phase is on liquidity and stopping cash outflows to avoid bankruptcy and create a solid cash flow position. To create positive cash flows, retrenchment steps such as closing down or divesting plants, and reducing headcounts might be inevitable. Hambrick (1985), however, points out the potential negative effects of retrenchment on internal morale and stakeholder support.

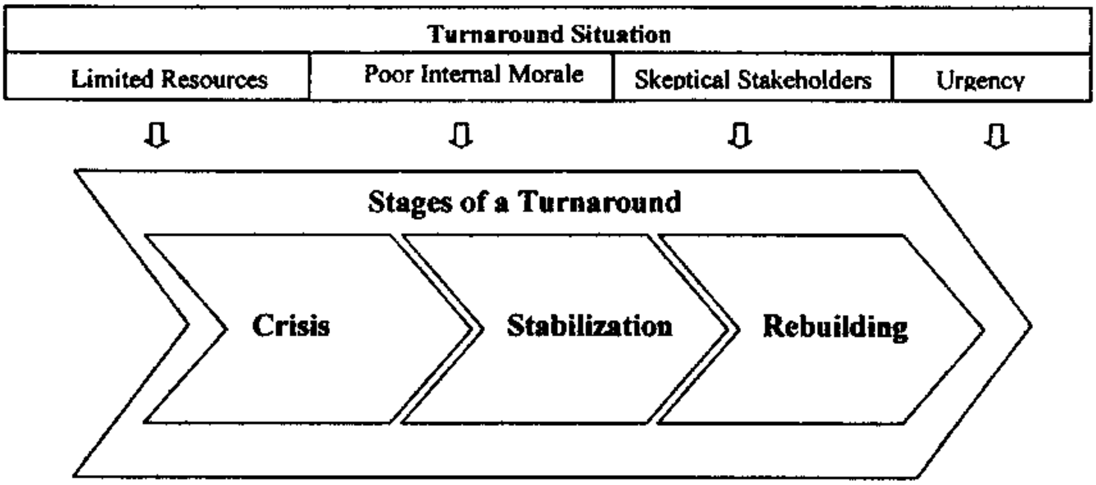

Figure 2: Contingency View on the Turnaround Process
Source: Author's Depiction based on Hambrick (1985)

If the survival of the firm is mainly secured as a result of liquidity and cash flow enhancing actions taken in the crisis stage, the firm enters the *stabilization phase*. In the stabilization phase the primary aim is to get "breathing room" (Hambrick, 1985:10-4). Attention in the stabilization phase is directed towards increasing margins, fine-tuning the production mix, targeting high-return market segments, and increasing the organizational efficiency to build up resources that can subsequently be used to lead the firm to growth. Control and information systems should be installed or improved. Management actions remain operational in the stabilization phase.

Finally, in the *rebuilding stage*, management attention shifts from operational issues to reconstructing the firm and returning to a growth strategy. In the rebuilding phase, entrepreneurial activities such as new product development, marketing campaigns, and asset renewal and expansion can be started or accelerated. The rebuilding phase is similar to a general strategic management situation once the impact of the characteristics of a turnaround situation i.e. the limited resources, poor internal moral, skeptical stakeholders and urgency of decisions have gradually diminishes and ultimately vanished.

Overall Hambrick (1985) focuses his process model on the action phases assigning less weight to recognition-oriented aspects. The model includes the contingencies that impact the turnaround process and thereby conceptually separates strategic management from turnaround management. Modeling the contingencies furthermore allows Hambrick (1985) to develop a deeper understanding of the stages in the turnaround process. The effects of retrenchment, for example, turn out to be positive only if assessed solely in the light of liquidity and cash flows. If internal moral and stakeholders are considered, the overall effect of retrenchment can become negative. Correspondingly, the conclusions of Hambrick (1985) concerning retrenchment strategies is, that they should only be pursued carefully, also taking the negative effects of decreases in internal moral and stakeholder support into account.

Hambrick (1985) fails to explicitly address the interrelations of actions taken in the crisis phase and the rebuilding phase. It is assumed that the rebuilding phase deals with ordinary strategic management issues independent of earlier phases of the turnaround process. If valuable resources are retrenched in the crisis phases, however, they are lacking in the rebuilding phase. Accordingly, subsequent researchers have questioned the assumption of independence between the turnaround process phases (Arogyaswamy, Barker and Yasai-Ardekani, 1995). Additionally, it becomes apparent, that Hambrick (1985) models human resources mainly from a cost perspective fitting the liquidity argument.

2.1.3 Retrenchment as the Foundation of Turnaround

In a rather extensive body of research, Robbins and Pearce propose a model of the turnaround process (Robbins and Pearce, 1992; Pearce and Robbins, 1993; Robbins and Pearce, 1993; Pearce and Robbins, 1994), which is derived partly from preceding work of

Bibeault (1982). Robbins and Pearce find, that the turnaround management literature up to the 1990s has appreciated the existence of retrenchment as part of the turnaround process, however, without thoroughly investigating the importance and value of asset and cost reducing strategies. Consequently, Robbins and Pearce investigate in their research the value of retrenchment for firms in turnaround situations.

Robbins and Pearce (1992; 1993) argue that retrenchment is not only a measure to enhance the liquidity position of a firm (liquidity argument), but much more an efficiency increasing action (efficiency argument). If costs are reduced and inefficient assets are sold off, the overall/average efficiency of the assets of the firm increases.

The general propositions of Robbins and Pearce are firstly, that the turnaround process consists of two stages – retrenchment and recovery. The separation in two stages draws from Bibeault's (1982) separation of focus between liquidity and growth in the turnaround process. Secondly, the turnaround management literature should predominantly focus on retrenchment since retrenchment and not strategic renewal is found to be the predominant determinant of successful turnarounds (Robbins and Pearce, 1992; Pearce and Robbins, 1993)

Turnaround situation severity is included as a contingency in the turnaround process model, drawing from Hofer (1980), who found in a case study of 12 poorly performing firms that a link exists between turnaround situation severity and the degree of cost and asset reductions necessary to achieve turnaround. Conditions of stakeholder support and internal moral are not explicitly modeled.

Similar to Bibeault (1982), Robbins and Pearce (1992; 1993) argue, that the two main objectives for a firm in a turnaround situation are survival and attainment of positive cash flows. To achieve positive cash flows, the distressed organization has to engage in typical retrenchment activities lowering cash outflows and improving the liquidity position through liquidation, divestment, product elimination, and head count cuts (*retrenchment phase*). These actions are based on the assumption that in the short run cash inflows from operations cannot be increased and a situation of low liquidity can only be resolved through lowering cash outflows. In the *recovery phase*, the aim shifts to growth and development. Means for the firm to accomplish organizational growth and development are acquisitions, new products, new markets and increased market penetration.

The two stages in the turnaround process are partially intersected (see figure 3). In the retrenchment phase, the firm seeks to stabilize the declining performance and weak liquidity and cash flow position by cost and asset reduction. If a satisfactory performance level is reached, companies can return to growth in the core business, but might still decide to divest in other business areas. The firm is at a decision point between the two stages (Robbins and Pearce, 1992; Pearce and Robbins, 1993): Either the organization can pursue recovery maintaining the preexisting strategy in a retrenchment-reduced form or change the strategic orientation. Robbins and Pearce (1992) argue that independent of the decision to change the strategic orientation, retrenchment is universally an appropriate reaction in a turnaround situation. They propose two major turnaround strategies: either an operating/ efficiency turnaround in which the preexisting strategy is maintained and the turnaround is achieved through asset and cost reductions and a diminished resource base or strategic/ entrepreneurial turnarounds in which retrenchment is the foundation for an altered strategic orientation for the return to sustainable growth.

Robbins and Pearce (1992) test their two-stage turnaround process and the integral part of retrenchment in the turnaround process. They investigated 32 publicly held textile manufacturers during the time period 1976-1985 and find that retrenchment activities during the turnaround attempt are positively related to turnaround success. For some firms retrenchment and resulting efficiency gains were found to be a viable turnaround strategy corresponding to the operating efficiency turnaround.

Firms encountering severe turnaround situations needed to pursue cost retrenchment as well as asset retrenchment. Firms facing less severe situations sufficiently reacted by retrenching costs. Cost and asset retrenchment together resulted in the highest average level of turnaround performance.

Based on their empirical findings, Robbins and Pearce (1992) derive their process model and conclude that retrenchment can be considered a core element in the turnaround process. Robbins and Pearce (1992) similar to Bibeault (1982) model the turnaround process from a financial/ liquidity perspective including a cost perspective on human resources without explicitly taking other contingencies into account.

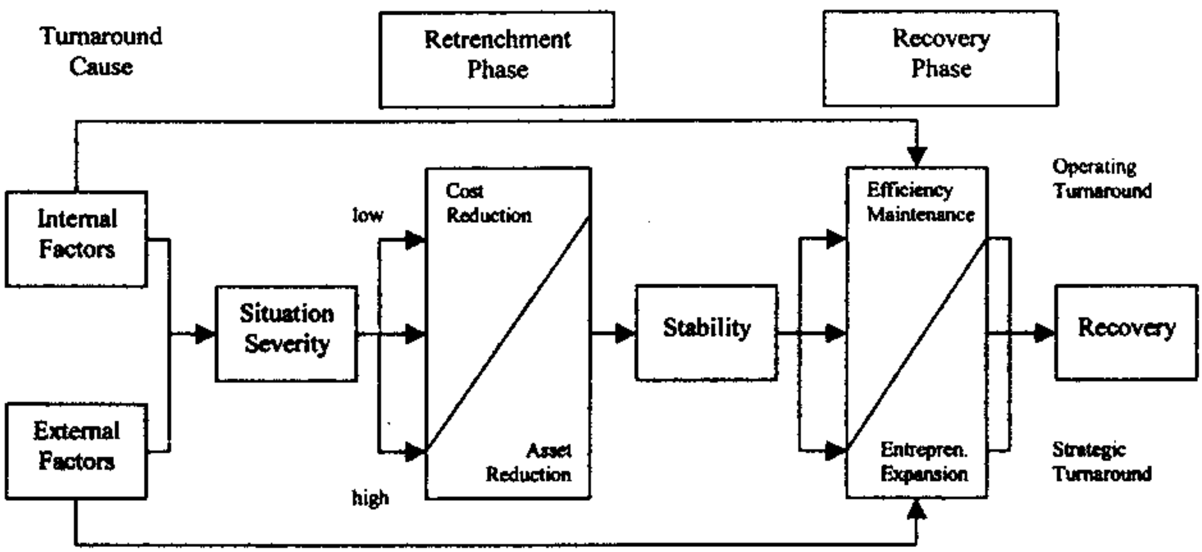

Figure 3: Retrenchment-based Turnaround Process
Source: Robbins and Pearce (1992)

Accordingly, they find a high utility of retrenchment activities, since negative effects of retrenchment are neither modeled nor considered. Especially the proposition that retrenchment in itself can be a strategy to achieve turnaround and that accordingly strategic renewal is less important than retrenchment has provoked opposing positions in studies raising both methodological and theoretical concerns (Arogyaswamy, Barker and Yasai-Ardekani, 1995; Barker and Mone, 1994; Barker and Duhaime, 1997). Accordingly, the view of Robbins and Pearce (1992) has lost its position as the dominant paradigm in contemporary turnaround research.

2.1.4 Towards an Integrated Turnaround Process Model

Most of the models present in the literature explicitly or implicitly focus on retrenchment as an initial management response to performance decline (Bibeault, 1982; Slatter, 1984; Finkin, 1987; Robbins and Pearce, 1992; Pearce and Robbins, 1993; Robbins and Pearce, 1993; Pearce and Robbins, 1994). The notion underlying this argument is that initial cost and asset reductions are necessary to counterbalance the cash outflows to avoid corporate failure. Empirical evidence that the retrenchment-focused researcners cite comes from studies that show turnaround firms becoming more efficient after retrenchment activities while recovering (Schendel and Patton, 1976; Hambrick and Schecter, 1983; Ramanujam, 1984; Robins and Pearce, 1992).

Arogyaswamy, Barker and Yasai-Ardekani (1995) and Barker and Duhaime (1997), however, argue, that the retrenchment-efficiency relationship proposed in large-sample studies may not necessarily be grounded in management-initiated retrenchment. The large sample studies measured ratios dependent on sales[2], so that rather than interpreting the improved ratios as efficiency gains, they can be interpreted as showing revenue growth. It is, therefore, unclear whether the efficiency gains are a result of retrenchment efforts, increased sales or a combination of both. The conclusion, however, that retrenchment is always positively related to turnaround success cannot be derived from studies using ratios dependent on sales.

Retrenchment is assumed to be a reaction to firm inefficiency (e.g. Bibeault, 1982; Finkin, 1987; Robbins and Pearce, 1992; Pearce and Robbins, 1993; Robbins and Pearce, 1993; Pearce and Robbins, 1994). Prior research, however, indicates that declining firms face severe problems additional to inefficiency such as dysfunctional decision-making processes (D'Aunno and Sutton, 1992), deteriorated firm climate (Hambrick 1985; Cameron, Whetten and Kim, 1987) and reduced stakeholder support (Hambrick, 1985). Therefore, retrenchment is under-specified to explain the initial response to decline (under-specification argument).

[2] Ramanujam (1984) and Schendel and Patton (1976) measured cost of goods sold/sales; Ramanujam (1984) and Hambrick and Schecter (1983) measured inventory/sales and receivables/ sales; Hambrick and Schecter (1983) additionally measured marketing expenditure/sales; R&D expenditure/sales and sales per employee.

One important contingency for the turnaround process is the cause of decline (Schendel, Patton and Riggs, 1976; Starbuck, Greve and Hedberg, 1978; Hofer, 1980; O'Neill, 1986a; Stopford and Baden-Fuller, 1990), which some process models failed to consider. Moreover preceding process models are linear and sequential and therefore unable to capture the interdependencies of turnaround process stages and the complexity of the process.

Addressing some of the criticism of prior turnaround models, Arogyaswamy, Barker and Yasai-Ardekani (1995) propose a process that includes turnaround situation contingencies and does not necessarily lead to retrenchment responses but rather to decline-stemming strategies. Arogyaswamy, Barker and Yasai-Ardekani (1995) reconcile in their theoretical contribution the stagnation and strategic management perspectives on turnaround in an integrated process model (see figure 4).

The two-stage contingency model proposed by Arogyaswamy, Barker and Yasai-Ardekani (1995) assumes that the declining performance of the firm is a result of either misalignment with the firm environment, environmental hostility or a mixture of both. If the decline is not turned around it can lead to erosion of external stakeholders' support, increasing inefficiencies in the firm, and worsening of the firm-internal climate and deterioration of decision-making processes. A declining firm fails when a combination of these consequences depletes the resources of the firm and causes the stakeholders to withdraw their support.

Two contingencies influence initial decline-stemming strategies: firstly the severity of the performance decline and secondly the level of organizational slack available at the time of the turnaround attempt.

The *severity of the decline* influences to what extent erosion of stakeholder support, inefficiency and deteriorating internal moral threaten the survival of the firm. The effect of turnaround-situation severity on decline-stemming strategies depends on the level of organizational slack. Organizational slack is defined as available manpower and/or financial resources. In situations of low *organizational slack*, firms facing severe performance decline are most vulnerable and as a result these firms are expected to pursue decline-stemming strategies more intensely. High available slack may on the other hand reduce the need for decline-stemming strategies. As slack can absorb variability in firm performance, it can protect the firm at least temporarily against dysfunctional effects of decline.

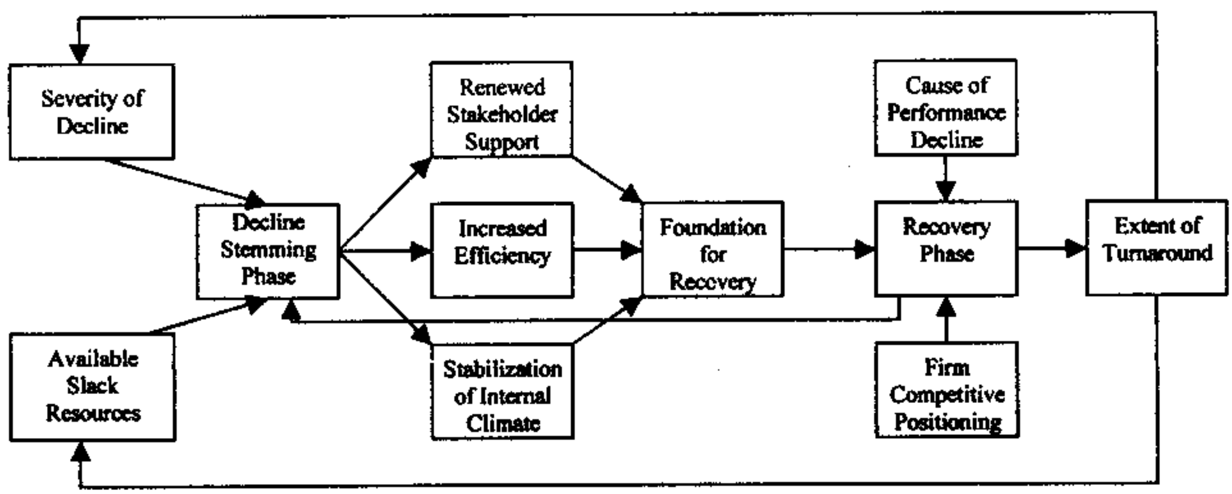

Figure 4: Integrated Turnaround Model
Source: Arogyaswamy, Barker and Yasai-Ardekani (1995)

Performance decline over a longer period of time stains the reputation of the firm and leads to deteriorating external relationships. Declining performance and deteriorating *stakeholder support* can lead to further decline, decreasing revenues, increasing transaction costs and reduced management flexibility (cf. Hambrick, 1985; Hambrick and D'Aveni, 1988). Revenues are often reduced as customers and agents seek new suppliers fearing e.g. that products may not be delivered on time. Often, maintained stakeholder support comes at an increased price, e.g. higher interest rates for loans, as the risk to support the firm increases. Firm flexibility suffers as other business partners impose restrictions such as cash-on-delivery or rigid terms for keeping credit lines.

In their turnaround process model, Arogyaswamy, Barker and Yasai-Ardekani (1995) propose that decreasing *efficiency* is the consequence of decline (and ultimately of ineffective strategies) rather than the cause of decline. Often declining firms suffer from reduced sales revenues as the demand for their products decreases either due to industry contraction or decreasing market share. Inefficiencies – defined as a result of an underutilized asset and cost-base as well as the increase of fixed costs spread over total production – decrease the competitiveness of the firm and erode the competitive position accelerating the performance decline.

Deterioration of the firm's *internal climate* restricts the ability to use human skills and assets to compete effectively with rival firms. Because of the unfavorable firm-internal environment, skilled employees may exit the organization taking valuable, firm-specific knowledge with them.
In addition, the restricted decision-making process potentially hinders top management to initiate organizational change. If the decline requires fundamental changes within the firm, shifts toward more mechanistic structures as a result of the decline may further restrict the firm's ability to adapt and address the causes of performance decline.

Arogyaswamy, Barker and Yasai-Ardekani (1995) propose the initiation of *decline-stemming strategies* to reverse or restrain the consequences of stakeholder support withdrawal, inefficiencies and low internal moral. Decline-stemming strategies constitute the first stage in the turnaround model and can be either external or internal in direction. External strategies stop the erosion of stakeholder support and renew the trust in the top management. Internal strategies create efficiency and stabilize the internal environment.

The first aim of the decline-stemming strategy is *stakeholder management*. The strategy seeks to change the image that the stakeholders have of the firm in a way that either increases or at least maintains their support.
The second aim of decline-stemming strategies is to eliminate *inefficiencies*. Increased efficiency by definition allows declining firms to better utilize their assets and cost

structures, which stabilizes the competitive position of the firm to some extent by lowering costs, improving cash flows and reducing the risk of insolvency in the short run. Increased efficiency may be a result of retrenchment, downsizing the firm, increased sales or a combination of the three. The methods used to increase efficiency in declining firms may vary depending on what recovery strategy is chosen by the management.

The last goal of the decline-stemming strategy is *stabilization of the internal climate and decision processes.* Arogyaswamy, Barker and Yasai-Ardekani (1995) argue that firms can avoid the mechanistic shift in structure and decision processes if the top management enforces a decentralization in structure, experimentation and free flow of communication. They also suggest that employee involvement counters the mechanistic shift and helps to maintain a positive internal climate. Additionally, uncertainty among employees due to expectation of downsizing measures can be reduced, if the top management maintains open communication during the turnaround attempt.

Arogyaswamy, Barker and Yasai-Ardekani (1995) stress the interconnectedness of the three consequences of decline and also the difficulties that firms may have to implement decline-stemming strategies that control and reverse all three decline consequences. The authors argue that, for example, the implementation of retrenchment plans without considering all organizational consequences may lead to reduced employee morale and commitment, increased employee alienation and withdrawal of the most talented and skillful employers. Retrenchment may create incremental or short-term efficiency gains and liquidity relief, however, in the long run such one-sided decline-stemming strategy may accelerate the deterioration of the firm's internal climate and decision process resulting in the dissolution of the firm. Accordingly, the authors go beyond the liquidity argument and address the competencies that personnel might have leading them to assess that retrenchment might pose severe negative effects.

Recovery strategies are the management actions and policy changes that seek to cope with the causes of the firm's decline and turn around performance to acceptable levels. Successful recovery strategies build on decline-stemming strategies - stakeholder support, increased efficiency, and stabilized internal environment – and also take into account the cause of decline as well as the firm's competitive position in the industry.

Recovery strategies can be described along two dimensions. Firstly, the extent to which strategic reorientation is a precondition for the recovery strategy and secondly, the extent of firm contraction or expansion involved in implementing the recovery strategy.

The extent of the strategic reorientation is a result of the recovery strategies and indicates how much the firm's strategy, structure, control and power distribution are altered during the turnaround attempt.

The *cause of performance decline* directly influences the need for strategic reorientation. Organizational research proposes that firms suffer decline either because of industry contraction or because of poor firm-specific adaptation to the internal and/or external environment (Tushman Virany and Romanelli, 1985; Virany, Tushman, and Romanelli, 1992).

Decline as a result of industry contraction occurs when the industry as a whole shrinks. The contraction reduces the number of firms in the industry, and most firms suffer from performance decline as they all compete for a reduced customer base.

In contrast, firm-based decline occurs when the firm is not sufficiently aligned with either its external or internal environment and consequently performs worse than the average firm in the industry.

The *stages in the turnaround process* are interdependent rather than sequential. The interdependency between both types of strategies, decline-stemming and recovery, means that they need simultaneous consideration. However, it also means that success at only one activity is not sufficient for turning the firm around. Initial or ongoing success either of the decline-stemming or recovery strategies creates conditions that facilitate the success in other stages.

The process model by Arogyaswamy, Barker and Yasai-Ardekani (1995) comprehensively incorporates relevant turnaround contingencies, and reconciles much of the preceding work on turnaround process and crisis situations.

This turnaround process model differs from other models in including different views on the turnaround process into one model: Efficiency oriented ideas of Robbins and Pearce on retrenchment are combined with stakeholder and internal perspectives stressed by Hambrick (1985).

2.2. Turnaround Strategy Content

This section reviews the turnaround literature from a strategy content perspective. A discussion of views on the cause of the turnaround situation, situation severity and the role of available resources are presented: Literature consistently found that turnaround strategies need to address the causes of decline (Grinyer and Spender, 1979; Hofer, 1980; Barker and Duhaime, 1997). Severity of decline influences the intensity with which turnaround strategies need to address the causes of decline (Arogyaswamy, Barker and Yasai-Ardekani, 1995). Available resources determine the top management flexibility to take certain actions.

Subsequently, turnaround strategy content is reviewed following the structuring dimensions of market-based view and resource/capabilities based view.

2.2.1 Turnaround Cause, Severity and Available Resources

Turnaround strategies differ from ordinary strategies, as they are dependent on the special circumstances that a turnaround situation imposes (Hambrick, 1985). Special conditions in a turnaround situation include a deteriorated internal firm climate (Hambrick, 1985; Cameron, Whetten and Kim 1987; Cameron, Sutton and Whetten. 1988), dysfunctional decision-making processes (Hedberg, Nystrom and Starbuck, 1976; Starbuck and Hedberg, 1977; Starbuck, Greve and Hedberg, 1978 Grinyer and Spender, 1979), potentially inefficient asset and cost utilization (Bibeault, 1982; Slatter, 1984; Pearce and Robbins, 1992; Robbins and Pearce, 1994) shrinking stakeholder support (Hambrick, 1985; Sutton and Callahan, 1987; Arogyaswamy, Barker and Yasai-Ardekani, 1995) and

– depending on the severity of the turnaround situation (Hofer, 1980) – a low degree of resources (Hambrick, 1985; Hambrick and D'Aveni, 1988).
Additionally, strategy content in turnaround situations should incorporate the long-term strategic goals of the firm that are set for the time-period after the turnaround has been achieved (Arogyaswamy, Barker and Yasai-Ardekani, 1995; Barker and Duhaim, 1997). If, for example, a company seeks to become market leader in a certain market niche during the recovery phase, the turnaround strategy should not incorporate a resource dilution of resources particularly tailored to compete in that specific niche market.

A group of researchers has categorized causes of decline as operational or strategic and has accordingly proposed operating or strategic measures for turnaround strategies (Schendel and Patton, 1976; Schendel, Patton and Riggs, 1976).
If firms face an *operative turnaround situation*, retrenchment is seen as an appropriate turnaround reaction (Hofer, 1980; Hambrick and Schecter, 1983; Finkin, 1987; D'Aveni 1989; Robbins and Pearce, 1992; Pearce and Robbins, 1993). Retrenchment as an operative turnaround strategy aims at increasing firm efficiency (Schendel and Patton, 1976: Schendel, Patton and Riggs, 1976; Hofer, 1980) and has therefore also been argued to be a general prelude and precursor for turnaround recovery strategies (Hall, 1980; Bibeault, 1982; Goodmann, 1982; Behn, 1983; Finkin, 1985). A group of researchers goes even a step further and argues based on the operative and strategic dichotomy of causes of decline, that in specific operating turnaround situations, retrenchment as response to performance decline is sufficient and might not require any strategic change (Hardy, 1990; Robbins and Pearce, 1992; Pearce and Robbins, 1993; Robbins and Pearce, 1993; Pearce and Robbins, 1994).
If the performance decline is rooted in strategic rather than operative causes, a *strategic change* or *entrepreneurial strategy* is needed in the purse of a turnaround attempt (Pearce and Robbins, 1994; Barker and Duhaime, 1997).
In sum, the continuum between strategic and operative strategic responses suggest strategic cures to achieve turnaround for turnaround situations caused by strategic misalignment with the environment and operating cures for turnaround situations rooted

in poor operational efficiency (Schendel and Patton, 1976; Schendel, Patton and Riggs, 1976).

The dichotomy between operating and strategic causes of decline has been supplemented and subsequently replaced by a structuring logic suggesting that the cause of decline can be either *industry-contraction based* or *firm based* (Arogyaswamy, Barker and Yasai-Ardekani, 1995).

General industry, market or market niche declines (*industry-contraction based decline*) can be caused by demand shifts to other industries, e.g. due to demographic changes or technological revolutions leading to new substitute products. As a result, the size or munificence of the industry in which the firm competes shrinks. The contraction of the industry or industry niche reduces the number of firms, which the industry can support and puts all or most industry participants in decline situations. The competitive pressures on all industry participants for a reduced resource base and profit potential increase (Whetten, 1987).

Resource and capability misalignments to the internal and/or external environment (*firm-based decline*) are independent of the size and profit potential of the industry in which the firm competes and are rather a result of organizational maladaption to market demands (Hedberg, Nyberg and Starbuck, 1976). The results of such misalignments are performance levels below industry average, which place the firm in a turnaround situation. Such firm-based declines can be a result of management failure to adapt the firm to changes in the industry (Zammuto and Cammeron, 1985). The incapacity of management to keep the firm aligned with the environment can originate in unanticipated changes in the industry structure, which lead to redefinitions of the source of competitive advantages. Alternatively or complementarily, competitive actions of firms may disconnect the resource and capability base of the firm from the competitive requirements that the environment imposes (Cameron, Sutton and Whetten, 1988). If the firm is placed through strategic reorientation, for example, in an industry or strategic group for which it lacks managerial skills or in which traditional assets, resources and capabilities are less valuable, such a strategic initiative can also be the cause of performance decline.

Deficiencies in corporate systems such as (capital market) communication systems, cost and financial control systems or quality management systems, furthermore can lead to deteriorating performance or late recognition of negative performance trends.

Hofer (1980) introduced the *severity* of the turnaround situation into the heuristic for selecting suitable turnaround strategies. Situation severity is determined by the magnitude, time frame and pattern of the performance decline (Chowdhury and Lang, 1994). Turnaround situation severity can be captured in the *resources available* (i.e. underutilized or additionally available human resources and particularly additional financial resources obtainable through increase in leverage of the firm), since a high degree of available resources makes the relative severity of a stiff performance decline low, whereas in a situation of low available resources, the relative severity of a gentle performance decline is high (Arogyaswamy, Barker and Yasai-Ardekani, 1995).
The flexibility of strategic responses to decline depends on the resources available to the troubled firm. If available resources are low, the flexibility to alter strategy content is limited, since neither financial resources, organizational competencies nor slack human resources are available (Thietart, 1988).

2.2.2 Market-Based View – Positioning School

The field of strategy content can be divided into the market-based view deriving generic strategies for the firm from the external competitive environment and the resource-based view. In this section the focus remains on the market-based view and in particular the positioning school. The subsequent chapter depicts the resource and capabilities view in turnaround strategy content.

The Positioning School seeks to identify attractive industries and favorable positioning in the industry (Mintzberg, 1990). Researchers have found, that although attractively positioned in a favorable industry or well positioned in the product-market lifecycle, patience and perseverance are not sufficient in a turnaround situation to achieve reversal of declining performance (Pearce, 1981; Pearce, 1982; Harrigan and Porter, 1983). If a firm is faced with a performance decline, although attractively positioned in an industry characterized by a high return potential, the cause of decline is not industry-contraction based but rather firm-based. If the firm is incapable of addressing the firm-internal causes of decline or if the firm is unable to increase the efficiency of assets and costs, the decline will persist. Consequently, inactivity is not an appropriate reaction to turnaround situations even if the generic positioning in the industry is favorable.

If the cause of decline is rooted in a permanent industry contraction, the same number of firms competes for a reduced resource base, which leads to increased competitive pressures and an increasingly hostile environment (Porter, 1980; Zammuto and Cameron, 1985; O'Neill, 1986a).

If the firm is well positioned in a declining industry, research suggests strengthening or holding the favorable industry position – at most implementing incremental strategic moves to target the most profitable remaining customers (Porter, 1980; Harrigan, 1985). This strategy encourages less favorably positioned firms to exit the industry, fail or retreat to smaller customer segments, reducing the overall industry capacity and thereby decreasing competitive pressures.

Research on the market-based view in declining industries suggests for weakly positioned firms in a permanently declining industry to selectively shrink to the market segments which allow for best leverage of firm capabilities (Porter, 1980; Harrigan, 1985). Niche strategies are favored over strategies that involve high levels of strategic reorientation, since weakly positioned firms lack the resources to initiate strategic changes and acquire the necessary capabilities to compete in distinct competitive positions.

If the performance decline is believed to be based on a temporary industry contraction rather than following a permanent downward trend, only incremental strategic changes that aim at strengthening the historic position of the firm are suggested (O'Neill, 1986b), since strategic reorientations bear a considerable risk of failure and are costly as firms need to learn new capabilities and routines (Hannan and Freeman, 1984). The costs associated with strategic reorientation are difficult to absorb in a declining industry

environment. Especially weakly positioned firms may be forced to shrink to a niche market segment in which the present capabilities can best be leveraged.
In order to investigate what positioning is favorable for firms in turnaround situations, researchers have inquired the relationship between structural variables derived from the structure-conduct-performance paradigm and turnaround success (Harrigan and Porter, 1983; Pant, 1986; Pant, 1991). The characteristic features of industries and firms that support successful turnaround are reviewed in the following paragraphs.

The likelihood for companies in turnaround situations to achieve turnaround was found to be higher for industries characterized by high R&D intensity (Schendel, Patton and Riggs, 1976; Pant, 1986). R&D intense industries hold the required industry dynamics that provide firms in a turnaround situation with the opportunity to alter their competitive positioning. R&D investments can increase the prospects of product innovations as well as productivity enhancing measurements (Schumpeter, 1934). As a result of product innovations, consumer demand may shift to the firm in a turnaround situation or industry structures may change providing the firm with an improved competitive positioning. Similarly, process innovations provide the opportunity to reduce costs and compete more effectively on price (Pant, 1991).

There is equivocal evidence that successful turnaround firms compete in industries characterized by low entry barriers (Pant, 1991). Lower levels of barriers to entry suggests that firms in an industry are not protected against competition, and they cannot raise prices to increase profit margins or compensate for inefficiencies in the cost structures, since new competitors would enter the industry. This could suggest, that high barriers to entry are related to turnaround success, because companies in a turnaround situation could explore price-increasing potentials. On the other hand, however, the opportunity to increase profit margins or raise prices is available to firms that aim at cost leadership or product innovation (Porter, 1985), both of which produce the industry dynamics necessary to reposition in the industry and achieve turnaround on that basis.

On firm level, relatively smaller firms were found to be more likely to achieve turnaround compared to larger counterparts (Pant, 1986). It is argued that smaller firms are more flexible in their structures and can therefore react to changes in the industry faster than larger firms. Also, less structural complexity may increase the possibility for speedier implementation of transformation measurements. In addition, smaller firms may have relatively less capital and therefore have to be more open to financial changes.

Also, operating profit margins are relatively lower for successful turnaround companies (Pant, 1986). A firm in an industry with low advertising expenditures may profit from an increase in its own advertisement (Comanor and Wilson 1979; Mueller and Rogers, 1980), however, this may cause present operating profit margins to decrease in the short run. Alternatively, a firm that invests heavily in technological development generates high development expenditures but also an improved likelihood for the achievement of technological advancement that alters the position of the company in its industry. These types of actions are typical turnaround boosters, although initially leading to lower operating margins (Pant, 1986).

There is only mixed support suggesting that turnaround firms generally have more recent growth and lower market share than non-turnarounds (Hofer, 1980; Harrigan and Porter, 1983; Pant, 1986; Pant, 1991). Arguably, firms that achieve turnaround pursue a strategy that aims at focusing the business into a narrower market segment, a niche. This argument would suggest that smaller market shares characterize successful turnaround firms. Contrarily, several studies present a linkage between market share and profitability based on economies of scale arguments (e.g. Schoeffler, Buzzel and Heaney, 1971; Buzzel, Gale and Sultan, 1975; Porter, 1980) suggesting that an increase in market share would be characteristic for firms achieving turnaround (Hambrick and Schecter, 1983).

2.2.3 Strategic Resources and Capabilities

The internal perspectives offered by the resource-based view complement the external perspective of the Positioning School especially since the 1990s (Wernerfelt, 1995).

Generally, firms that are faced with internal causes of performance decline need to implement strategies that realign firm-internal capabilities and resources with the internal and external environment (O'Neill, 1986a). The strategic realignment can be grounded in building or acquiring and exploiting strategic resources and capabilities.

If organizational capabilities and resources are misaligned with the environment, but the firm is competing in an industry with sufficient profit potential, the suggested turnaround strategy involves strategic redirections to build the firm internal resources and capabilities needed to compete more effectively in the industry. If the misalignment is a result of unanticipated industry-structural changes that shift the source of competitive advantage, an appropriate turnaround strategy needs to redefine the competitive position that is most promising and restore or create the internal resources and capabilities that allow the company to move to the identified position characterized by high profit potential. Correspondingly, a definition of the key industry requirements and key success factors is the starting point for the identification of a future capability set that the firm needs to acquire, build or transform to. Depending on the requirements of the industry, the turnaround strategy can incorporate imitating behavior (Grant, 1998).

The special circumstances of a turnaround situation, namely a diluted internal morale, dysfunctional decision-making processes, low available slack resources, internal inefficiency and shrinking stakeholder support, all serve to limited the extent to which resources and capabilities can be acquired or build. Therefore, the turnaround strategy falls in the continuum between the potential benefits of Ricardian or Schumpeterian rents, the cost associated with acquiring the necessary resources and capabilities (Grant, 1998), the costs of strategic redirection needed to reposition the firm to leverage the new resources and capabilities (Hannan and Freeman, 1984) and the risk of ultimate failure due to the limited availability of resources and withdrawal of stakeholder support (Hambrick, 1985; Sutton and Callahan, 1987; Cameron, Whetten and Kim 1987).
The turnaround strategy needs to consider the interdependencies between short-term activities, required resources and capabilities for a favorable strategic positioning as well

as leveraging potential (Barker and Duhaime, 1997) and the long-term strategic goals of the firm that persist over and above the time period of the turnaround attempt (O'Neill, 1986a; Gowen and Tallon, 2002). Accordingly, required resources bearing relevant competencies (such as human resources) need to be retained to keep the organizational capabilities in place to initiate growth after the turnaround situation is overcome.

3. Research on Turnaround in South-East Asia

Multinational corporations and financial investors have invested heavily in South-East Asia during the 1990s. The Asian crisis, however, lead companies to experience financial distress and turnaround situations. Imposing Western standards of turnaround strategies on South-East Asian joint ventures or equity involvements lead many companies to a further deterioration of performance indicating that the Western measures are inappropriate in an Asian setting (Backmann, 1995). Consequently, the question arises what elements of the western model of turnaround are applicable in South-East Asia and to what degree?

Management conventions impact the universe and evaluation of strategic alternatives (Weidenbaum, 1996). Correspondingly, differences in management conventions in different cultures result in different arrays of strategic alternatives and in different evaluations of strategic options (Weidenbaum and Hughes, 1996). Hence, culture shapes to some degree management actions.
Furthermore, cultural differences induce differences in the internal and external firm environment (Weidenbaum and Hughes, 1996; Bruton and Rubanki, 1997). Therefore, different strategies prove favorable in different cultural environments.

At this point it becomes important to make explicit, what the South-East Asian cultural environment refers to: In line with the studies on turnaround in South-East Asia by Backmann, (1999) and Bruton, Ahlstrom and Wan (2001) and with the argument, that management conventions impact strategic decisions, South-East Asia refers to ethnic Chinese businesses. These businesses are argued to have a dominating influence across

South-East Asia and to be homogeneous with respect to cultural characteristics independent of country borders (Backmann, 1999; Bruton, Ahlstrom and Wan, 2001).

The following differences between the Western business environment and the South-East Asian environment have proven relevant for the analysis of differences in the turnaround process and turnaround strategy content between South-East Asia and the West: ***organizational setup, management style, guanxi*** and ***maintaining the 'face'*** (Bruton, Ahlstrom and Wan, 2001).

In South-East Asian firms, the father or the oldest male member of the family is usually head of the family and the business, which results in a particular ***management style*** (Kao, 1993). The head of the family is powerful both economically within the firm and socially within the family. Family members or close relatives mostly hold top management positions assigned by the head of the family. The leadership style is rather authoritarian based on an unquestioned, unrivaled experience advantage of the head of the family. Management responsibilities are rarely handed over to family outsiders (Weidenbaum and Hughes, 1996).

The South-East Asian firm structures and organizational setups are mainly based on family relationships. The *family business* is a reaction to the weak contracting and law systems throughout major parts of South-East Asia (Weidenbaum and Hughes, 1996). The crossholdings of firms reinforced by family members in top management positions enhance the control over the various businesses within the firm as well as manages the tightly controlled information flows within the organization (Chen and Drysdale, 1995). The family structures result in complicated ownership and crossholding structures of South-East Asian firms and an intransparent network of stakeholders. Core businesses usually hold interest in dozens or more small- and medium sized firms (Weidenbaum, 1996).

Guanxi, connections and relationships, are important to South-East Asian and particularly ethnic Chinese business people (Standifird and Marshal, 2000). Time and effort is devoted to developing and maintaining these relationships. In a guanxi relationship all parties have to benefit from the transactions. Guanxi connects people by the exchange of favors rather than friendship and compared to Western business practices, the Chinese value long-standing commitments rather than signing contracts (Yeung and Tung, 1996).

In Confucian societies, shame is what prevents individuals from illegal or immoral behavior (Hawang, 1987). The key component is the emphasis on "*face-saving*". The face is more than just a person's reputation. In China, the face is compared to the bark of a tree; without the bark, the tree dies (Yeung and Tung, 1996). If a person looses face, this brings shame to the individual and to the family members putting both under social pressures. Guanxi is an important part of the face work, since the reputation of a person is established and maintained in the context of social interactions (Yeung and Tung, 1996).

Based on the incomplete list of differences between the Asian and the Western business environment, some incompatibilities between the Western and the Asian turnaround model can be highlighted, namely the ***recognition of decline***, ***ability to retrench***, ***CEO replacement***, ***speed of turnaround*** and ***matching of turnaround cause and response***.
Recognition of the turnaround situation regularly takes longer in South-East Asia, because of the organizational setup with a relatively intransparent governance system characterized by cross shareholdings (Bruton, Ahlstrom and Wan, 2001). Moreover, the decline situation is in tendency longer and with more persistence denied in an South-East Asian setting, since a turnaround situation induces face-losing for the responsible business man. Additionally, the guanxi networks allow the firm to explore additional available resources even if in a Western setting the leverage limit would have been reached. When the deterioration of performance becomes apparent, however, it is usually stiffer than in a western setting (Backmann, 1999).

The *ability to retrench* in an Asian setting is limited, since the South-East Asian companies are mostly labor intensive and located mainly in cheap labor countries. Generally, they therefore have a rather slim organization where efficiency increases through retrenchment are difficult to achieve (Bruton, Ahlstrom and Wan, 2001). Moreover, social factors such as the lack of a social security system in many South-East Asian countries and ethical factors such as the life-long employment maxim that still plays a role in many South-East Asian businesses limit the extend to which retrenchment is a viable operating strategy for a turnaround attempt.

Limitations are put on *CEO replacement* and reorganization of top management teams. Thereby the face of top management team members is maintained and the guanxi of the top managers, which form a valuable asset to the company, is secured. Also, it is considered difficult to replace family members on the board as it would damage their reputation. Consequently, managers are not replaced formally, rather the power shifts within the firm to other key personnel if the top management is found to be incapable of turning the firm around (Bruton, Ahlstrom and Wan, 2001).

The *speed of turnarounds* is much slower in Asia than in the Western world due to the intransparant organizational setup, the limited availability of retrenchment options and social conventions. The experienced urgency stressed very much as an important contingency in the Western turnarounds by Hambrick (1985), correspondingly, is lower.

Matching of turnaround cause and response has consistently been found in a Western context to foster recovery (Schendel and Patton, 1976; Schendel, Patton and Riggs, 1976; Hofer, 1980; Hambrick and Schecter, 1983). In South-East Asia, the cause of decline is mostly rooted in strategic problems, particularly in unrelated diversifications (Bruton, Ahlstrom and Wan, 2001). Therefore, (portfolio) restructuring measures can be expected to play much more of a role in South-East Asia as turnaround measure to address the cause of decline than retrenchment strategies (Backmann, 1999).

The very limited research published internationally that deals with turnaround in Asia already uncovers the fact, that generalizability of US and European findings to an South-East Asian environment is limited (Kang and Shivdasani, 1997, Bruton and Rubanki, 1997, Bruton, Ahlstrom and Wan, 2001; Gowen and Tallon, 2002).

In general, many business variables take different values in South-East Asia as the preceding paragraphs have shown. As a result of the differences in business variables, the Asian environment proves distinct from the Western environment inducing that Western turnaround concepts need to be reexamined for an Asian context.

4. Future Research Directions

The limited knowledge of the *turnaround process* in South-East Asia reveals important differences to Western models and shows that the Western process model is inappropriate and hence inapplicable in South-East Asia. The turnaround process in South-East Asia, therefore, is a fruitful area for future research inquiries.

Since the ability to address efficiency through retrenchment is limited, because the stakeholder support depends more on the guanxi and the long-term relationships of the business leader than on planned actions to manage the perception of stakeholders and since the level of internal morale deterioration is impacted by the particular authoritarian management style, it becomes apparent, that the decline-stemming phase of the turnaround process is fundamentally different in South-East Asia.

Guanxi might lead both internal and external stakeholders to show solidarity with the troubled firm, increasing commitment even if financial ratios already suggest withdrawing of support. Also, the authoritarian and centralized management style in South-East Asia might influence the extent to which decision-making processes during a turnaround attempt deteriorate as compared to Western situations.

All those factors clearly indicate that the Western turnaround process model is inappropriate in South-East Asia and induces, that a novel construct of the turnaround process for South-East Asia is needed.

The Western *turnaround strategy content* models have largely been driven by the liquidity argument and by a notion of operational turnarounds leading to the suggestion of retrenchment during turnarounds (although a solely retrenchment-driven turnaround is not postulated given the under-determination argument; Arogyaswamy, Barker and Yasai-Ardekani, 1995). Additional to the negative retrenchment effects on internal morale and stakeholder support discussed for a Western setting, retrenchment strategies are further restricted for South-East Asian companies for several reasons: Firstly, retrenchment cannot be implemented by many South-East Asian companies with slim organizations and facing social and ethical restraints (Bruton, Ahlstrom and Wan, 2001). Secondly, the liquidity argument is short-term oriented – an orientation that manager in South-East Asia do not need to share due to a higher degree of independence from capital markets. Accordingly, the South-East Asian managers can value the long-term detainment of organizational competencies concentrated mainly in the knowledge of the human resources (resource argument) and the value inherent in the interaction between the human resources (value argument) more than the short-term results and liquidity. The limited applicability of the widely applied concept of retrenchment in a Western context poses the question as to how far the turnaround strategy content in South-East Asia is similar to Western concepts.

Due to the limited applicability of Western turnaround strategy content concepts in South-East Asia, a knowledge gap exists in the turnaround literature. Accordingly, an investigation of the turnaround strategy content for South-East Asia is an important field for future research attention. A similar assessment is made by Bruton, Ahlstrom and Wan (2001:162), who highlight that "the nature of the turnaround actions pursued including retrenchment and strategic versus operating turnarounds all represent important topics for future consideration".

In sum, two research gaps in the turnaround literature are identified: Firstly, the turnaround literature has not produced a comprehensive process model accounting for particularities in South-East Asia. Secondly, the turnaround strategy content research has not uncovered the alternatives to retrenchment and hence a taxonomy of turnaround strategies applicable in a South- East Asian setting.

Future research might strive to address the research gaps to better understand the turnaround process and turnaround strategy content in South-East Asia, to recommend successful turnaround strategies and thereby to help avoid corporate failure and contribute to economic and social prosperity.

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