Restructuring – and improving business performance
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For a business to change its shape, how it operates, and how it behaves can be daunting. It is fraught with risk. But it can be – and is – done:

- to integrate an acquired business
- to restore profitability
- to change the operating model in a fundamental way
- to cope with changes in the market
- to prepare for eventual disinvestment.

Restructuring is not necessarily a fundamental overhaul of structure and processes. It can be a series of co-ordinated initiatives to improve the business’s performance. Carefully planned and skilfully executed, these can have as profound an effect on results as a major re-engineering programme.

This is not a manual telling managers what to do. But it does set out a number of related topics and discusses them in the context of successful restructuring. Relevant case histories get a mention where that is useful. We draw on our experience in different sectors.

We start with the challenge of a potential acquisition or major investment – the first period when a deal is done or a decision made to seek radical improvements in performance. We consider the framework for restructuring; and discuss discrete projects to tackle specific weaknesses or respond to new situations. The ‘nuts and bolts’ topics include how to change organisational structure, reduce costs, measure and manage performance, enhance profitability, improve marketing competitiveness, streamline procurement and supply, and change employment practices.

Planning and risks

Senior executives can make the most impact by drawing up a plan and designing the organisation to realise it. That inevitably points to the need to restructure. This is an opportunity to set new rules and change the wavelength throughout the company. But it can go sadly awry in the research, planning or execution. That’s why the main risks need to be evaluated, and managed out. The priorities need to be understood – and shared. And for that, a conceptual framework based on good practice is required.

Introduction

Collinson Grant has helped lots of businesses to restructure and improve their results – in the United Kingdom, in Europe, and in the United States. This document is an attempt to share our experience and to set out what we think is important.

“Change, change, why do we need change? Things are quite bad enough as they are.”

Lord Salisbury to Queen Victoria
In a company that still appears to be successful, the top executives will fight shy of seeking commitment to a radical restructuring. Why rock the boat? Then, when the boat is rocking, plans for change can miss the mark because they are heavy on theory and principle but light on practical experience. Many failures are put down to poor ‘strategy’. But it is more often in execution that things go wrong. Even modest plans can achieve great results if put into practice proficiently!

Restructuring is not just about redesign. This view underemphasises the importance of establishing a managerial team – albeit a temporary one – with the motivation, clear thinking and willpower to fire up radical change and drive it through. Victorious executives in take-overs often imagine that their team of stars is acquiring a set of duffers. But this is seldom the case. The most successful restructuring melds the best managers into a stronger team than either part had. The creation of this team – with a top executive handpicked for the job – can be one of the keys to success in complex restructuring.

New acquisition – shooting star or black hole?

The pressing questions for any potential investor are: Should we buy at all? and How much should we pay?

Many different aspects of a potential target merit investigation. But the potential buyer is likely to give priority to three. Each of them has a direct bearing on price:

- major opportunities – the ways in which the business could be improved. It might, for example, reconfigure the value chain; take initiatives to cut costs; sell unprofitable divisions; harmonise employment practices; slim the management team; or set up better controls
- principal downsides – internal and external factors that might affect the company’s prospects of improving its profitability in the short and medium term
- exit strategy – how the business might eventually be sold (and when), through an Initial Public Offering, trade sale or management buy-out.

An independent assessment of these factors should help investors to confirm or question an initial offer price. It should also provide a forecast of performance, which – evaluated against historical results – prompts specific actions.

Financial due diligence aims to reveal pitfalls hidden in the balance sheet. Operational due diligence should give a clear view of the target and a solid case for what it is worth. It should also tell the potential buyer what steps to take on purchase to achieve the profit forecast and to put the business on the right footing for eventual disposal.

Is diligence rewarded?

The limitations of financial due diligence are well known. Some big deals are struck after little formal investigation. In these cases, the price appears to have reflected the apparent increase in risk. A well-managed company in a regulated industry will seldom give rise to unexpected concerns. But one-off due diligence is often done with indecent haste. Keen executives tend to soak up the good news that reinforces their commitment to the deal, but to blank out problems that could lead to doubt. And the due diligence report itself is so hedged about with caveats, both buried and overt, that there would be little value in taking action against its authors.

By contrast, operational due diligence by practised hands can open a goldmine of useful information, analysis and experienced opinion. Of course, it too provides little legal remedy. But its revelations about the true standing of a business in the marketplace can be invaluable. And a thorough appreciation of culture and values as well as of the contractual conditions of the main employees can help to set the priorities for the personnel in the period straight after the takeover.

“A wrong decision isn’t forever; it can always be reversed. The losses from a delayed decision are forever; they can never be retrieved.”

J K Galbraith
Operational due diligence

There is a story behind every set of financial accounts – operational due diligence sets out to uncover it. No appraisal of a business can be completed without an understanding of how and where it makes money. So markets, customers and competitors must be investigated. How strong are the relationships? How stable are the economic conditions? How active are the competitors? Internally – How capable are senior managers? How robust are the core processes? How reliable are the managerial controls? And how well are costs controlled? Has the company invested in new technologies and kept up with the market? Are its employment practices in order? Or are there problems just beneath the surface?

The company might realise all the opportunities: or fall prey to every risk. The range between success and failure is wide:

It is important to act quickly and to collect and analyse information on completion of the deal so that the pre-acquisition judgements can be validated – or not!

The options for gathering data may be limited. Often, the purchaser may only:

■ examine and analyse the selected operational and financial data provided by the business
■ hold discussions with a few chosen senior managers
■ have a quick look at how the business is run and at the day-to-day culture and climate
■ gather and analyse information from brokers, analysts, competitors, the trade and other sources.

Accurate information may be hard to find. So it is important to be selective in deciding what is and is not pertinent. Information should be weighed and analysed only to shape decisions on the likely risks of acquisition, on the opportunities to improve the business, and on possible exit strategies. Many investigations reveal inconsistent reporting and incomplete data. Plugging the gaps in due diligence is time-consuming, and may well not be cost-effective.

Due diligence also gives an early opportunity to ‘see and feel’ how the business works.

The familiar signs of a vulnerable organisation

■ Micromanagement by the boss
■ Too many layers
■ Narrow spans of control
■ Tendency to by-pass the manager, and work directly with the manager’s manager
■ Layers defined by pay, status, or grade, not by work content
■ The employee does not feel the manager adds value to her/his work
■ The employee thinks the manager talks too abstractly, without enough specifics
■ Lack of leadership – too much or too little guidance
■ Poor communication between employee and manager – too much or too little information

A powerful database interface can be used to interrogate the available information and to highlight vital signs. For example, reports can indicate the relative profitability of product groups and market segments, and the trends in costs and performance. Even when full access has been granted, it is not unusual for managers to be reluctant to reveal all the data or to hinder their collation.

An impending takeover can be a time of great uncertainty for the managers and staff. Key people may decide to jump ship. Others will jockey for position. Some may choose to be less than co-operative. Profitability often drops. The company’s capabilities, its market standing, skills and knowledge, can be irreparably damaged.

“"There was no telling what people might find out once they felt free to ask whatever questions they wanted to."

Joseph Heller – Catch 22

Annual profit

Current profitability

Maximum opportunity realised

Highest factored risk

Range of opportunity / risk

Reality?

Expectation!

Time

Exit

Acquisition

Range of
profitability
Restructuring after an acquisition – the first quarter

The deal is done. The banks are in position, their covenants subtly crafted, the papers signed in myriad copies. The lawyers relax. The new management team walks through the door of its latest investment. This is the moment of truth. Now the quality of the preparation will be sorely tested. That ominous quotation: ‘Two-thirds of all acquisitions fail to meet the investors’ expectations’ rears its head.

If you have been there, you will know the feeling. Will you arrive to find the banners out to welcome a saviour? Or will it be the deathly hush of condemned men awaiting the hangman? All this depends on how you prepared the ground and did your investigations. Are you confident about those first critical steps? Or are you relying on instinct and bravado?

First impressions – Whatever you do and say, this first impression will last. There is an important element of theatre. The first contact with the managers and staff gives a unique chance to set the future tone. This is the chance to act out the values and culture of a new business, and to show how you want it to work.

The plan – There needs to be an inclusive plan for the first quarter. Three distinct managerial tasks need to be kept in balance:

- to keep ‘the show on the road’ (management of the business)
- to make short-term improvements to achieve the profit forecast
- to set up the plan and the structure for the next three years.

Four types of control – How should the acquired business be managed? McKinsey describes four ways:

- operational independence – few decisions are required. Only the accountabilities of the most senior managers need to be confirmed
- takeover – the acquirer’s managers take charge of the new business and impose their own processes
- merger of equals – the best aspects of both businesses are selected
- transformation – the whole is expected to outperform the sum of the parts.

If an acquisition has unique capabilities and resources that can provide competitive edge, it may be wise to let it keep some freedom. For a large acquisition, it may well be best to adopt specific managerial styles for different parts of the business.

But if an acquisition has poor finances, processes or people, the acquirer may well choose to isolate it until improvements are made. That way, it will avoid infecting its own business. And an acquisition in an unrelated business may also be kept separate rather than integrated.

In contrast, companies that are similar may be integrated to achieve economies of scale and scope. The acquirer may subjugate the acquired company, or both may be merged into a new identity. Or there may be benefits in remaining separate but sharing skills, capabilities, knowledge or technology where there is an opportunity to do so. In these cases, combining back-office or operational functions can be practical – and a great source of savings.

Whatever the strategic imperative, success will depend on establishing an ambitious but credible plan thatplaits the three strands of managerial attention. All three demand well considered communication with every member of the workforce, every customer, and every supplier. For they will all wonder what is going on. And they will all assume the worst!

“Get your facts first, and then you can distort them as much as you please.”
Mark Twain
Framework for managerial action

A framework for restructuring and integration is set out opposite. It highlights three strands of activity:

- Managing risk
- Implementation
- Strategy

“No institution can possibly survive if it needs geniuses or supermen to manage it. It must be organised in such a way as to be able to get along under a leadership composed of average human beings.”

Peter Drucker
Reorganisation is a top-down activity. In summary, the main steps are:

- Understand the context and policy
- Set the scope and managerial authority for making change happen
- Define outcomes and objectives – financial returns
- Confirm the project management framework
- Complete a thorough appraisal of the business
- Establish effective communications – with all interested parties
- Allocate sufficient resources to manage the changes and minimise risks
- Research all the options and analyse the data
- Define the new business model and value chain
- Create a structure of accountabilities – with metrics and managerial nodes
- Complete the organisational structure
- Decide what information is required
- Confirm systems to support decision-making
- Implement specific improvement projects – to reduce costs and improve service
- Manage redundancies and the re-allocation of employees and duties
- Tackle outstanding problems on personnel/employee relations/pay.

Maintaining momentum

Plans and tactics evolve as more and more is known about the business, its customers, its abilities, and its main cast. Although the original rationale for the deal will provide direction and a focus for action, managers must be prepared to challenge the business case and adapt as circumstances change and information accrues.

The main players – Who really will make a difference? Not just the senior executives, that’s for sure! Who will play a leading part in the new business? It is vital to find out. It is easy to be impressed by smooth talkers. But success can often depend on people behind the scenes. They may have a rare expertise, or deep relationships with key customers or suppliers.

At the same time, the framework for measurement and control and the plan for restructuring are formed. The business should be appraised against a comprehensive checklist. Ways to improve operations and to cut costs must be devised, modelled and tested. Some tasks will be relatively easy to do and should provide the much heralded ‘quick wins.’ Others will require a lot more investigation, appraisal of the impact on customers and, often, well reasoned arguments to overcome the resistance of managers and others. All this takes time. So a good project manager is a must – to keep things on track and to react to unforeseen snags.

Above all the business has to keep going. There needs to be reliable, timely and consistent financial and operational reporting in place as soon as possible. This cannot be taken as a given. Every business has its own rules and protocols for compiling the managerial accounts. Until these are understood, and accepted, every report should be treated with caution.

Communication is a high priority. Customers, suppliers and employees all have a right to know what is going on and that their interests are being protected. The planning phase should include the best way of communicating carefully crafted messages to each of the priority groups. Good practice demands that as much communication as possible should be face-to-face.

And there are strategic decisions to consider. A decision is not strategic just because it is complex or ‘grand’ in conception. But it is strategic if undoing it would take a great effort, or would have a big impact on the company. By this test, many decisions that are strategic are made without adequate investigation or consideration. In contrast, too much time may be spent debating matters that could be reversed in days with little risk. Special care is needed to determine which matters are truly strategic, because those decisions may well have to be delayed.

Immediate actions to manage the risks

1. Set up the short-term executive team:
   - clarify personal accountabilities for achieving the immediate profit and cashflow forecasts
   - highlight the interim nature of this team
   - assess the need for special short-term rewards for beating the short-term forecast
2. Go through the balance sheet, cash position and management accounts with a fine-tooth comb
3. Confirm any short-term liabilities
4. Investigate the veracity of the forecasts for short-term sales, net profit and cashflow
5. Resolve, with the executive team, how best to achieve the forecasts, even with reduced sales, by making short-term cuts in cost
6. Establish cash controls and effective managerial reporting
7. Cross-reference these findings to the due diligence reports and highlight any urgent actions
8. Establish extra interim reporting arrangements quickly, if necessary
9. Prepare initial communications to customers, employees, investors and suppliers to gain their understanding and co-operation
10. Speedily assess the business’s true market position through personal visits to meet the principal customers and sample survey of others, emphasising a listening approach – before taking any significant action with marketing or sales plans, organisation or strategy
11. Visit the main suppliers to assess their capability and reliability
12. Evaluate the quality of processes, systems and methods of operations
13. Summarise all these findings in a short report for co-ordinated action.

“There are risks and costs to a program of action. But they are far less than the long-range risks and costs of comfortable inaction.”

John F Kennedy
Organisational structure and its implications

An understanding of how business organisations should work is a useful starting point in restructuring them.

All businesses hover in a constant state of flux. They have to keep on adapting to changes: in market conditions; in the ambitions of their owners; and in the economic climate. So they can end up with a structure that patently does not work. This shows in lots of ways. Managers and employees are not really sure what they are supposed to be doing. Processes act against the interests of customers rather than for them. Responses to problems are hit and miss. And the controls that should spur on the gallant entrepreneur actually hold him – or her – back.

Restructuring offers the chance to put things right and to think carefully.

**Capability** – What should the new organisation be capable of doing?

**Accountability** – Will managers know what they have to achieve?

**Possibility** – What are the realistic options for a new structure?

**Feasibility** – What constraints might hinder the pursuit of the best solution?

**Flexibility** – How quickly could or should changes be made?

Any major restructuring is most likely to take place in stages. The big bang approach, though sometimes necessary, is fraught with danger. Most businesses, if they have the option, will tackle back office systems and other non customer-facing operations first. Only when this change is bedded in and seen to be working properly is it safe to start improving the commercial facets of the business.

To set the agenda, how fast does the business have to adapt:

- to achieve the tough targets for growth set by executives and investors?
- to respond to rapid technological change in products and services?
- to cope with steep decline as a result of changes in the marketplace?

How well do senior managers make radical change? What lack of skills might put plans at risk?

The organisational structure translates agreed strategy into tangible results: to manage assets, control resources and create value. Most of all it should provide a framework in which people can excel and contribute positively to the success of the business. And it should have the ability to renew itself, to adapt to emerging situations, and to respond to changing circumstances. Given that structure has a major influence on cost, it will also affect competitiveness and profitability.

Many firms have high inertia. They remain bogged down in archaic and costly structures, with out-of-date processes and poorly trained employees. Worst of all, their managers lack imagination and fight shy of risk. Such companies find it hard to change.
A balanced approach to organisational design

A business keeps its balance only when each component of the structure responds to the evolving strategy and to changes in the other elements. To define an overall structure, it is necessary to determine managers’ accountabilities and responsibilities; fully specify jobs; design processes to meet customers’ needs; and apply powerful but simple controls to monitor performance and prompt the right managerial behaviour.

The elements depend on each other. Wherever in the cycle you alter the status quo, you should consider what changes in structure, accountabilities, processes or controls that initiative will bring in train – and what effect they will have on the underlying culture and values.

Structure and accountability

Organisational charts frequently do not reflect how a business actually works. In fact, an extensive, informal grapevine of communications, influences and alliances often complements, and contradicts, the formal channels. Nevertheless, the prescribed structure has a major influence on managerial behaviour and sets the framework for costs and accountabilities. It can provide the differentiating factor for competitive advantage, if designed with sufficient understanding of the market and of the strengths and weaknesses of the business.

The structure also takes account of the core business processes and systems, and illustrates to everyone in the company how it measures profit, generates gross margins and controls costs. Managerial controls need to integrate power and authority with responsibility. They can provide powerful levers for encouraging managers to perform better and for rewarding excellent performance.

Organisation, culture and values

A programme of restructuring depends on a thorough appraisal of the business and its culture, people and history of change. What values, behaviour and structures – both formal and informal – maintain the culture? A series of diagnostic tools can be used:

- to characterise the prevailing managerial style
- to recognise the nature of the controls in the business
- to establish the efficiency of the formal structures and the informal networks
- to determine the resources available to promote change and any likely shortfalls, and
- to recognise the initial sources of commitment or resistance to change.

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Recognising core business processes

There is a natural tendency to organise businesses around common skills and types of work – sales, production, purchasing, finance et cetera. This makes departments easier to control because managers are supervising employees with experiences and competences with which they are familiar. This arrangement is also a sensible approach to the co-location of similar assets and facilities.

However, the core business processes that determine the competitive performance of a business usually span more than one department. So there is a strong counter-influence to structure the business around the few, but important, processes that ensure that customers’ needs are met. This minimises the loss of momentum, quality and managerial accountability that can occur at the artificial interfaces between departments.

This approach also prompts a systematic analysis that:

- highlights each main task and its supporting activities
- establishes the costs of aggregated tasks and the main elements of each process
- allows a cost model to be developed, indicating the sensitivity to fluctuating volumes
- suggests where and how managerial controls should be deployed.

In large, non-devolved businesses and in non-commercial organisations there is often a compromise between the ‘vertical and functional’ and the ‘horizontal and process’ strands. Some managers will have dual responsibilities, but their critical managerial accountabilities (and key performance indicators) should be closely linked to the efficiency, effectiveness and outputs of customer-driven processes.

“Perfection of planned layout is only achieved by institutions on the point of collapse.”

C Northcote Parkinson – in Parkinson’s Law
Shaping the organisation

Although there are many different organisational designs, they can be grouped in three main categories – each different in the way that accountabilities are defined.

It can be helpful to set out three approaches to organisational design:

■ the devolved organisation – emphasising the profit centre
■ the integrated organisation – with separate customer-facing and internal structures
■ a hybrid structure – which combines different elements in order to match particular market conditions.

Profit centres

How and where profit is to be managed and measured is a principal factor in organisational design. This leads to the underlying concept of the profit centre – a self-contained, relatively autonomous unit whose leader (chief executive, managing director, unit manager or even depot manager) has to achieve a budgeted net profit. Profit centres can be large – effectively encompassing all the operations of a business – or small, where a company is subdivided into a number of separate units. Profit centres are the fundamental building blocks. They clarify where profit is measured, who manages it, and who manages cost.

Disparate business activities are best organised in this way. The managing director of each trading entity should have the authority to set prices and for marketing and selling; as well as for providing the products and services. This approach has simplicity and encourages entrepreneurial behaviour. It allows maximum responsiveness to local markets, gets decision-making closer to the customer and creates the facility to link managerial incentives directly to profit.

However, it can degenerate into a patchwork of fiercely independent territories that, in the extreme, compete with each other. There can be other significant downsides:

■ ineffective application of the company’s total resources
■ minimal exploitation of economies of scale
■ poor, and sometimes misguided direction
■ minimal sharing of ideas and experience.

The integrated organisation

The alternative to autonomous profit centres is the division of a business into separate functions, some customer-facing, and some supporting. ‘Commercial’ units, generating margin, are separated from ‘operational’ units providing products and services. They differ from profit centres in the managerial approach, style and values they need.

Monitoring performance requires some form of transfer pricing between the internal ‘supplier’ and ‘seller.’ More complex businesses will have a chain of internal suppliers. These arrangements can become a source of conflict, prompting disruptive behaviour that jeopardizes the profitability of the total business. A functional mindset can override commercial priorities. But, effectively implemented, separate commercial and operational units offer powerful incentives for managers.

This approach can help:

■ to clarify managers’ accountabilities by providing clear measures of performance
■ to simplify accounting and the measurement of margin and profit
■ to strengthen relationships with customers through more focused commercial activities.

Transfer pricing reinforces the strategy, sets out the managerial disciplines, and underpins the underlying culture of the business. It requires firm rule-setting from the centre and can help in applying a strong downward ratchet on costs. There is benefit in using transfer prices set at actual or targeted unit costs that incorporate fully absorbed overheads. Margin is best not ‘shared’ or ‘allocated’ between commercial and operational units, as this obscures accountability.
However, this apparently simple principle is fraught with practical difficulty for implementation. It can be hard:

- to decide who should be accountable for each part of the value chain
- to determine the basis for creating unit costs – and to stick to the rules
- to establish how transfer ‘prices’ should be maintained
- to work out how margins should be calculated and monitored
- to investigate the impact of changes in product and mix on the underlying cost base.

A ‘hybrid’ structure

The hybrid organisation – essentially a matrix structure – can have two, or more, strands. One may be focused on products or technology, the other designed to exploit particular market segments. The potential weakness of such a structure is the conflict that can arise when one person reports to two bosses.

However, the looser structural form helps to deal with complexity and has particular advantages. It can foster creativity, provide the right conditions for teams to thrive, and help them and individuals to act maturely and take decisions effectively. It can adapt quickly to changing markets, and can handle complex tasks done by numerous specialists. But it can also blur objectivity, hinder effective decision-making, reinforce bureaucracy and undermine accountability.

There are some pointers to success.

- Responsiveness, speed and clarity should be the primary objective.
- There should be clear – concise but not bureaucratic – rules about what each axis of the structure can and cannot do.
- People should accept that they will have to cope with uncertainty and shifting relationships, because they usually serve less stable markets.
- Some cultures do not readily accept more ambiguous forms of control.

Hybrid structures may well be temporary in nature – adapting to changing circumstances in the market, to the adoption of new product groups, or to the preferences of senior managers. Although they can be harder to control from the centre, this should not be an excuse to abandon the format or change it too frequently when problems occur.

Embedded costs – Layers and spans

The ‘shape’ of an organisation does a lot to determine its effectiveness and cost. Wide, flat structures tend to be more efficient than tall, narrow ones. Many firms have loads of people with managerial status (and pay) but no clearly defined managerial responsibility. This results in higher costs, slower responses, and lower productivity.

Having fewer managerial layers makes for flatter and more cost-effective structures that facilitate communication from the top to the bottom and from the bottom up. Flatter structures focus accountability more sharply because they delegate less. More layers spread and diffuse the responsibility for measurable outputs. Managers should be responsible for the work of others. If they do the same tasks as those they manage, they are more likely to be ‘team leaders’. Those who do specialised work or are classed as ‘expert’ and manage or supervise no or few others should not be called managers but placed elsewhere in the structure.

“‘It is not the strongest of the species that survive, nor the most intelligent, but the one most responsive to change.’”
Charles Darwin

“If sufficient number of management layers are superimposed on top of each other, it can be assured that disaster is not left to chance.”
Norman Augustine
Former CEO – Lockheed Martin
Reducing costs is not necessarily a specific task in itself. It should be an outcome of the various restructuring initiatives under way. However it is handled, a solid framework of measurement should be in place. This means — if at all possible — knowing the precise costs of functions, processes, products and any other activities before any action is taken.

People remain the largest single cost for many businesses. To recognise that you have too many people is one thing. To do something about it is another. But how do you find out where resources are being used inefficiently and where too many people are doing the same thing?

**Process activity analysis**

Process activity analysis provides a powerful technique for reducing overhead costs. A systematic survey of key processes, activities and tasks, it quickly reveals overlapping activities, redundant effort, and work that offers little value to the business but that incurs high costs. Process activity analysis allows managers to make informed decisions when the scale of the changes dictates a more fundamental approach to reorganisation and makes job losses necessary. It constitutes an essential tool for restructuring core processes.

This approach shows how costs can be reduced without diminishing the overall performance of the business. It provides a plan for reducing the indirect, staff-driven cost base. The initiative should win the commitment of the managers accountable for those costs.

Process activity analysis confronts the problem directly. The benefits are threefold.

1. It is based on questioning and gathering data from the people in the business itself. In other words the solution has the merits of being ‘home grown.’

2. Most members of the project team are from the business itself, which scotches the suspicion that it is being ‘done over’ by outsiders hired to eliminate jobs. Nevertheless, the approach is robust and is led by experienced practitioners.

3. The process has an excellent record as the most penetrating and least damaging way of reducing the staff. Trades unions will endorse the methodology, once persuaded of the managers’ resolve to take action.

Process activity analysis interrogates the staff not only by managerial or functional allocation (department by department) but also, more importantly, by processes and activities. It asks ‘What do people actually spend their time doing?’ rather than ‘Which department do they sit in?’ We have found it revealing to examine costs as:

- **Core** – adding value to products and customers
- **Support** – needed to maintain the organisation
- **Improvement** – required to change and improve the business

Typically, support costs should be in the region of 20%, improvement activities no more than 5%, and 75% of overall effort concentrated on adding value.

The data are collated, tested and stored in a robust database. This provides for multi-dimensional analyses of different variables. The results often cause considerable surprise — giving managers a different perspective on operations and processes that they thought they understood well. This evidence informs decisions on how to reduce costs. It usually pays dividends to take considerable time to convince managers of the need to act.

“It requires a very unusual mind to undertake the analysis of the obvious.”

Alfred North Whitehead
(British mathematician)
Taking the approach of a new entrant

A new entrant into a sector can have a number of advantages – new ideas, products, processes and IT, lean overheads, and – perhaps best of all – a willingness to consider what used to be unthinkable. But what it lacks are relationships, a history of supply, and a record that can be trusted.

What does this say about the status quo? If the business is successful, everyone may be loth to rock the boat. If it works, why mend it? But processes age quickly. Technology and IT get better and cheaper. So it does not make sense to wait until change is forced on the firm. Radical changes to the whole system that have been put off for too long may be rushed through, raising costs, alienating customers, losing sales – and ending in a profit warning.

It is far better to get the staff to work out, with specialists, what the processes could be like if the firm were to become a new entrant. Properly handled, there is little risk for employees. It is ‘blue-sky’ thinking. But the investigations and dialogue can throw up ideas on how to achieve much of the benefit with limited disruption. A business with various sites, products, and customers can pilot new processes without ‘betting the bank’. When such experiments do not work well, they raise the willingness to experiment, and offer the chance to learn from mistakes.

Much of this can be done out of view of the market and with little financial risk. Trying out new processes in a small way before applying them generally can achieve as much as barnstorming initiatives to re-engineer that take more time and run more risk.

Analysing and mapping processes at the right depth

Many managers see process mapping as mundane and beneath them. It is true that it has to be done and documented painstakingly. As in many managerial tasks, the doing is as important as the output. The act of mapping can open the analyst’s eyes to the opportunities for improvement. Those who do the work that is being analysed are sometimes shocked to find so many activities that are inefficient and waste time. ‘I assumed that x was dealing with that...’ or ‘Doesn’t y make sure that’s right?’ are frequent responses.

However, such insights only come about if the analysis and mapping are set at the appropriate degree of detail. It is tempting to analyse every bit of each procedure and process in great depth, without considering their relative importance or frequency. This kind of problem arises when changes to IT systems are afoot, and all the users wish to have everything they handle suitably automated. Not only does this make the processes much more complex, it also diminishes flexibility to a point at which even minor changes in inputs and outputs cannot be accommodated without major upheaval.

Redesigning business processes

Everyone knows that lots of businesses get their basic ways of working wrong. They are inefficient, inaccurate, expensive to administer, and badly managed and controlled. What is to be done? Well, just overhaul and redesign these processes, build them into a suitable structure, and Bingo! A new and vibrant company can be set up. Or so it goes.

In practice, ‘Business Process Engineering’ worked best on firms at death’s door. In these, it was easier to get the managers’ commitment. Because the alternative was so dire, drastic change could be rushed through. Some well-known firms invested heavily in this new approach – Proctor & Gamble, Hewlett Packard, Southwest Airlines and lots of others.

But there is more to a business than its processes. A firm often has to set up a new top team to take it forward before it can even think about re-engineering. Keen leaders pick the key people who know how things actually work and are willing to switch them round. Refreshed, the firm can then go to market as a new entrant. This has its attractions. But it has risks too. When an acquirer who does not really know what he has bought changes the processes and prices willy-nilly, he can bewilder the customers, cheese off the employees, and turn a goldmine into a millstone.

“Complex processes are by their very definition rigid, inflexible, low quality and high cost.”

Michael Hammer
The solution is to prioritise the processes to be mapped and to decide how deeply to document them. Analysis will reveal nothing if it is too shallow. But it will bury any revelations in unmanageable detail if it is too deep. In doubt, it is better to do the shallower analysis first, and then to use this to find the critical points at which to dig more deeply.

We advocate the use of proprietary software, so that all those involved can be familiar with a single set of protocols and their outputs. These systems can be used flexibly, as the users choose. Inefficiencies and rework can be presented in a simple model showing the flows and losses at various points.

The quality of that presentation is important, because visualisation can influence judgement. A long-serving technique known as ‘brown-papering’ emphasises this well. In this, all the documents and reports being analysed are attached to a single piece (usually a roll) of brown paper with arrows and lines showing the links and relationships between documents and data. This is then usually displayed around a single room or across a floor – with dramatic impact.

In this, all the documents and reports being analysed are attached to a single piece (usually a roll) of brown paper with arrows and lines showing the links and relationships between documents and data. This is then usually displayed around a single room or across a floor – with dramatic impact. It shows complexity, repetition, errors and rework in a way that a single sheet of paper does not.

Opportunities for improvement

It is tempting to initiate a process-mapping investigation with a team of ‘experts’ or, at least, outsiders. But the managers and staff who have run the system for years may well feel defensive when asked why the problems have been allowed to fester, aggrieved that their opinions are not valued, and fearful that a new method will be imposed. We have found that a mix of those who do the work and the analysts provides the best chance of success. It is essential to provide suitable training for the whole team to help build rapport and trust, and to assure a consistent approach.

How the project is set up makes a big difference to the sustainability of the change. It helps if the people who work with the processes are enthusiastic about the outcome and fully appreciate the chance to improve. Involving them closely in the investigations and design will help them to see the potential benefits. The commitment of the staff – and managers – who have been included in such a way is often remarkable.

Mapping the influences on costs

The temptation to form premature theories upon insufficient data is the bane of our profession.”

Sherlock Holmes

Appraisal of work content

This approach allows managers to build up a cost model from first principles. It is sometimes known as ‘zero-based budgeting.’

An accurate evaluation has to be made of what work needs to be done in a defined period: how this is broken down into different tasks; how long each task should take; what allowances should be built in for supervision, management, training, absence etc; what support functions are necessary (HR, finance, purchasing) and what their cost will be. A useful starting point is a map outlining how customers are served, what separate cost centres are involved, what the main drivers of costs are, and the key processes.
Employment practices

Large reductions in costs arise from major change – when fewer people are required than before and/or when the nature of the work becomes radically different. But when this happens it also affords an opportunity to review employment practices and to resolve long-standing anomalies and inconsistencies. It should cover:

- **Pay drift** – poor controls on pay inevitably lead to higher than planned costs. ‘One-off’ benefits are always worthy of further examination.
- **Recruitment and selection** – in many companies, poorly co-ordinated recruitment processes lead to duplication and higher costs. In tight labour markets managers seriously underestimate the cost of finding recruits.
- **Unproductive time** – the analysis will reveal the proportion of time being spent on meetings, travel, managing e-mail, social events and other activities of questionable benefit. The underlying rationale must be challenged.
- **Use of temporary and contract workers** – many firms run with lots of agency workers, but fail to find out their costs or to manage their performance. What employment rights do contract workers have? Why have managers pursued this policy?
- **Overtime (paid or unpaid)** – too much or too little use of overtime indicates that people have been poorly apportioned to tasks. There should always be slightly more work than people to do it.
- **Managerial time** – a comparison of how managers in different parts of the firm use their time can be revealing. Signs that they spend a significant amount of time on the same tasks as subordinates should be examined.

A simplified approach includes these steps:

“The model of costs can be compared with the actual costs, but this does not necessarily reveal where and how savings should be made. The review should encompass core processes, procurement, overheads, technology and employment practices. Most improvements are likely to accrue from a small number of critical sources.”

“A simplified approach includes these steps:

- Improve processes
- Remove duplication
- Eliminate redundant tasks
- Change structure

Greater productivity
Fewer jobs
Less wasted work
Better focus
Confirmed projects
Savings plan

“Theoretically, this should provide a robust model to find out the best size and shape of the business and hence its cost. However, it relies heavily on managers describing precisely what work needs to be done and how much effort is necessary to do it. There is a real risk that the very inefficiencies and duplication that should be revealed and eliminated in order to reduce costs might be actually endorsed and embedded in the revised structure. This is particularly the case when the work is complex, with few repetitive transactions and no directly relevant comparators. Judgements tend to be made on subjective criteria rather than on objective reasoning.

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“Some people will never learn anything because they understand everything too soon.”

Alexander Pope

Shakespeare (Hamlet Act IV Sc. 5)
Measuring performance – controls and reporting

Effective controls and reporting underpin every successful business – they should be a cornerstone of any major restructuring programme.

It is helpful to be clear on definitions:

**Metrics** are ways of evaluating performance, often in the form of ratios and indices that relate two or more variables, with an accepted scale or unit of measure.

**Controls** are the reports, and other means, that are used to communicate performance to managers in a way that allows them to take action.

The flow from measurement to action is:

Metrics » controls » analysis » diagnosis » action

The sequence must fit together to achieve the goals of the business.

First, set a few clear aims to boost performance, each one linked to the results of the whole organisation. The fact that the relevant data may be difficult to collect should not be a deterrent. Each of these objectives should show in some way whether or not the business is winning (or losing!). This simple expedient results in a limited number of ‘decisive performance indicators’. They are decisive because they should be all that is needed to direct the activity.

There should be a hierarchy of measures, so that the ones at operational level tie in with those that monitor policy and financial performance. This is illustrated in the diagram:
Too many KPIs?

It is easy to be overwhelmed by the plethora of targets, key performance indicators, indices and variances. So many managers find themselves juggling their activity to meet different measures. This is made more perilous by the perception that many may change in importance on each reporting occasion.

Performance is measured because ‘what gets measured gets done!’ But the temptation is to measure what is easily measured, not what needs measuring. There are some useful tests of the quality of a reporting regime:
- how relevant are the measures to the overall performance of the business?
- do managers have adequate control over the performance of the activity on which they are measured?
- are there just enough measures or are there too many?
- are the data on which performance is reported robust – that is consistent, appropriate, economic to collect and auditable?
- is the reporting timely (both in-time and on-time) so that corrective action can be taken?

Benchmarking – opportunities and risks

Benchmarking has sometimes been seen as the solution to many of the problems of target setting.

“We know that performance is inadequate but no-one believes us! So if we find a credible external comparator, we should be able to gain the buy-in of those whose job it is to get results!”

Comparing performance can have benefits. But the functions and processes chosen need to be similar enough for comparison to be seen as fair. The benefits of benchmarking appear as much in the doing as in the end results. No firms are identical, but elements – processes, sectors served, products, services, capital employed, headcount, and space, for example – can be directly compared, given access to reasonable data through desk research, co-operation, benchmarking clubs or synthesis. But this may just result in the firm’s catching up while competitors forge ahead. This very attitude – ‘the follower’ – can result in the adoption of ideas, innovation, strategies and plans that are not thought through, leading to a ‘me too’ philosophy and a loss of individuality.

Collection and analysis of data

Computer systems appear to provide the panacea for many, if not all, of the ills of data-collection and analysis. But the data obtained for a specific purpose, though readily available, may yet be totally inappropriate. New processes for collecting and analysing data may be needed for a specific index or measure. So carefully controlled sampling might be a much better option. This is particularly helpful when a new performance index has to be implemented quickly and there is no time for reprogramming, testing and debugging. The statistical validity of a sample needs to be tested, but is frequently higher than would be expected.

For data to be effective, the people collecting and analysing them should:
- explicitly define each element and formula so that those who use the data do not spend unfruitful time in disputes about definitions – a data dictionary is valuable
- make innovative use of the current ways of collecting data, without duplication
- avoid clerical work and manual recording wherever possible
- assure integrity and in-process validation (it is not possible to ‘inspect’ quality into the process!) collect and report on time.

Balanced scorecards

The challenge in reporting a number of performance indices is to assess whether an improvement in one is comparable with that in another. At a high degree of sophistication, it may be practical to build an econometric model that combines the results mathematically. But the creation of such a formula may not be justified. It may demand too many good data, and too much testing.

Balanced scorecards can be used to good effect. The indices in the chosen set are each given a (usually estimated) weighting to reflect their relative importance. A set of, say, ten indices can be combined into a single score that indicates a clear trend. Movements in the trend can be investigated by studying the changes in the various indices.

Outline framework for a balanced scorecard

<table>
<thead>
<tr>
<th>Objectives</th>
<th>Indices</th>
<th>Units</th>
<th>Performance</th>
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<tbody>
<tr>
<td>Financials</td>
<td>a Sales</td>
<td></td>
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<td></td>
<td>b Gross margin</td>
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<td></td>
<td>c Cash</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Customers</td>
<td>a Satisfaction</td>
<td></td>
<td></td>
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<td></td>
<td>b Churn</td>
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<td></td>
<td>c Acquisition rate</td>
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<tr>
<td>Internal processes</td>
<td>a Error rates</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>b Productivity ratios</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>c Cost reduction rate</td>
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<tr>
<td>Learning and growth</td>
<td>a Capability framework</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>b Qualifications</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>c Development projects</td>
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</tbody>
</table>

The weightings of the indices, and the indices themselves, can be changed to reflect changes in circumstance. This results in a discontinuity in any graphical representation, but it does give managers the flexibility to concentrate effort on emerging factors. However, misunderstanding and conflict may arise if the indices or weightings are changed willy-nilly, or without consultation with those whose performance is being measured.

Benchmarking

“We both married above ourselves. We both have trouble with the English language. We both have big biceps... well, two out of three ain’t bad.”

George W. Bush comparing himself with Arnold Schwarzenegger
Performance bridge

A performance bridge shows the movement from one set of numbers to another. It has several potential applications during restructuring. The aim is to agree on a ‘baseline’ and then to explain and summarise differences, for example:

■ by the contribution from different business units, sector markets, geographies, sites/plants, lines of business, etc
■ by root cause – price, volume, gross margin, overhead cost reduction, etc
■ by individual initiative within a programme of many restructuring projects.

Performance bridge: major projects

The performance bridge is a powerful means of holding the restructuring team to account and ensuring that the investment in bringing about radical change is worthwhile.

Used in conjunction with a project ‘scorecard,’ it should be aligned with the normal period management accounts to explain the effect of other unforeseen variances and/or changes of tactics. Comparison of the performance bridge projected at the outset of a restructuring exercise with the final picture will show to what extent the initial plans have been translated into firm, measurable results.

“IT’s clearly a budget. IT’s got a lot of numbers in it.”

George W. Bush

Budgeting to boost profit

Most firms can improve their profitability. But the most profitable can be the least productive!

It all depends on how the high return on capital employed has been achieved. Some businesses sail on a calm sea of successful products, loyal customers, attractive markets and wide margins, with no rivals to ruffle the waves. They see no risk. Only when the competitive Kraiken wakes do they find that they are not seaworthy in rough waters. Holed by underinvestment, then abandoned by their customers, they can be swallowed up.

Growing markets may seem to offer ready profit from increased volume. But a huge investment in products and processes may be needed to achieve it. Only a thorough knowledge of the market will reduce the risk of being misled about the sustainability of the profitability and cashflow.

Making budgeting exciting

Successful companies have ways to set ambitious targets and to reward key people fairly. These spring from rooted norms and values. Setting budgets can be painful, unrewarding and frustrating – a battle between managers and their bosses. Several unproductive iterations may result in a horse-traded compromise.

The setting of bonuses can also influence the targets for profit or sales. Each manager tries to hide away as much ‘undeclared upside’ as possible.

The whole process can be made more relevant and productive.

■ Work through the sales forecasts with their expected gross margins. This will reveal the profit gap. To bridge it, adjust pricing (to flex gross margins) or cut costs, or both.
■ Do not inflate sales above what can reasonably be expected. That leads to disaster. Secure in the expectation of big sales, managers let overheads balloon. So, when the sales forecasts are missed, overheads are excessive for the volume.
■ Set a modest yet realistic sales forecast. Drive down overheads to achieve the required profit. Any surplus sales immediately boost profit. Investment in new ideas, products and projects is made possible.
■ With appropriate preparation, it is possible to prepare the budget at a three-day conference. If all the senior managers are present, the whole thing can be done and dusted over a weekend. And that gives the entire team a rosy glow.

Metrics not Es

Managers preparing budgets tend to set themselves tougher physical measures than financial ones. It is possible to base a budget on prepared and researched physical ratios (which are then converted at specific rates to total costs).

In one large distribution business, the whole of the budgetary process was based on forecasts of ratios, such as units per drop, miles per drop, drops per day, trips per vehicle, annual stock turns by item and so on. The resultant budget was so tough that the central finance function made provision to cover what it feared would be the performance gap. Very little of it was needed!

Equivalent units, considered later, are used with some of these elements to create a culture in which year-on-year reductions in real costs are the norm, not just a nice idea.
Improving operations

Fundamental restructuring prompts an examination of the total business model and every aspect of operations. The analysis centres on increasing productivity and maximising profit.

Re-examining the value chain

- What are the core capabilities that give us competitive advantage?
- How do our customers expect us to serve them?
- Which components/products would it be better to procure externally?
- Where should we manufacture and/or assemble?
- What skills are required for manufacturing or providing a service – and do we possess them?
- What are the risks of an extended supply chain?
- Is a partnership or alliance a sensible approach?

The answers determine the shape of the organisation and where initial activity should be focused – on improving internal operations or finding external partners. They will prompt questions on structure, capability and location – where should tasks be done and by whom? Or – how can the performance of the existing model be enhanced?

Back to basics

When you walk around an operational unit, what do you see? A hive of activity? Numbers of people in huddles? Raw materials and work in progress in abundance? Notice boards full of graphs and exhortations? Machines and processes set ready to work? Lots of technical paperwork? An exciting sense of crises being resolved? Is it possible to know how well it is really going?

So much manufacturing has been transferred to South East Asia and Eastern Europe that the United Kingdom is losing its expertise. The financial services industry too has been exporting jobs in administration and service (mainly in call centres). Senior managers can find themselves responsible for an operation in Europe or India that they feel uncomfortable managing. Such deals, once struck, can take years to unpick.

Inefficiency shows up in many easily observed ways:

- Untidiness and poor housekeeping
- People walking about or standing in huddles
- Lack of clarity in the flow of work
- Badly categorised orders and materials
- Lack of quality control
- Badly marked out work flows, gangways and storage areas
- Out-of-date graphs, announcements and reports on notice boards
- Poor timekeeping and attendance
- Dirty washrooms and toilets(!)

Inefficiency shows up in many easily observed ways: Complex reporting lets managers hide basic inadequacies. Reports on service can wrongly highlight the manager’s perspective, not the customer’s. Unit costs can reflect only the mix of products at the point of study: weightings need to ensure that the results reflect actual practice.

Measuring the trends in total unit costs and the profitability of products shows better than any reports on efficiency whether operations, in its own right, is competitive.

Lean operations

A specific effort to boost performance in an operational unit can have startling results. Applying ‘lean’ principles to operations can help them:

- to make effective use of space and equipment, marking unused areas off to avoid encroachment
- to organise speedy changeovers to cut downtime
- to separate products in large batches from those with short or infrequent runs
- to allocate materials, components and part-finished products in fixed amounts to marked areas
- to prepare simple documents that anyone with limited experience can follow
- to provide visual aids that make progress clear
- to show clearly the productivity of processes and labour and the material yields
- to promote team-working.
Using a ‘lean’ training programme to cut costs
A company wanted to use training in lean manufacturing to give managers the skills to investigate every element in the business’s Value Chain. They could then use that learning to specify and ‘charter’ projects to improve working practices and to reduce costs. The business wanted to find cost savings of 42.5 million Kroner or 5% per year and to cut inventory by 61.0 million Kroner.

The management team followed a structured programme, which allowed them:
- to define the project, to set priorities and to determine internal resources
- to review the current situation, assess performance and map processes
- to decide upon the ideal future state and develop the projects necessary to achieve this
- to prioritise the projects and develop charters setting out measurable targets, customers’ requirements and resources.

‘Lean’ techniques were used to focus activity on processes where most improvement could be achieved and to harness the enthusiasm, skills and experience of the workforce. This included assessing customers’ needs, mapping the flow of materials and information, reviewing data on performance and costs, measuring lead-time and capacity, and investigating errors. Managers also investigated the suppliers, measured their performance, and recognised components and processes that might be outsourced.

Nine separate projects were outlined, with considerable potential to cut costs, reduce inventory and improve order lead-time. They embraced better purchasing, selected outsourcing and specific improvement in processes and working practices. Total projected savings were in excess of the target.

Outsourcing – a boon or a bind?
Europe and the United States increasingly depend on adding value through design and services, leaving the outsourcing manufacturers to supply products to explicit specifications. But design works best when those who market the product are close to designers who have a thorough understanding of the latest processing technology and capability. Outsourcing manufacturing may undermine this ‘development team.’

A designer and a process engineer several thousand miles (and cultures) apart cannot have the same relationship as two people who see each other every day.

Outsourcing and sub-contracting have become something of a panacea. ‘Our own business does not do it well, but there must be someone out there who can do it better!’ And that may be true. But it does not follow that that is the best decision.

The drive to cut costs, especially of labour-intensive items, has immensely strengthened South East Asia. China in particular has covered a list of world-wide manufacturing. But its infrastructure and logistics put it at risk. And there continue to be real fears about the loss of trade expertise and technology.

‘Plans are only good intentions unless they immediately degenerate into hard work.’
Peter Drucker

Job in services are easier to relocate, given that many of the outcomes of their work are in an electronic format that can easily be switched from one continent to another. In call centres, language becomes another big consideration. Not all outsourcing ventures by large banks have been successful. Services for directory enquiries are among several that are prone to cultural misunderstanding.

The desire to concentrate on a specific market, product, or geographic area ebbs and flows with the perceptions of competition and risk. Given the time it takes to move from concentration to diversification (or back), the timing of the decision is the key to success.

However, there is a strong trend towards capital investment and expenditure on refining processes. It is seldom economic for the single business to maintain world-class expertise in several technologies. Each must decide which horse to back.

Outsourcing is a decision that can take years to reverse. When a business jettisons its manufacturing, it may become just a distributor competing in a different market. While that may be the intention, it can have unexpected consequences that turn out to be irreversible.

Considerations for outsourcing

The decision whether to outsource part or all of manufacturing poses some fundamental questions of strategy:
- How important is operational expertise to our business?
- Can we outsource a component or ingredient of our product?
- Can we retain enough expertise to manage the new supplier so that quality is not compromised?
- What impact will this have on our marketing stance?
- Will we be able to serve our customers in the same way – and will they notice or care?
- High-value items can be sent by air, but many others need to go by road or sea. What impact will this have on our responsiveness in the market and our ability to modify or customise products?
- Will this result in the price paid by our customers falling? What effects will that have on our relative and absolute margins?
- What will be the true annual savings per year, taking into account potential reductions in sales prices, increases in supply chain costs, rises in working capital and loss of responsiveness?
- Is our proprietary technology, intellectual property or expertise at risk?
Profitability of products, customers and markets

Products, customers and markets can each yield a wide range of gross profit margins. Finding out why helps to refocus the business and improve profitability.

Low-margin products often absorb more overheads than are fully accounted for. So it is helpful to analyse the profitability of each product. Then managers can decide: to adjust the price, cut the costs, apply value engineering, or delete the product altogether. A specialist database interface can reveal valuable information about the profitability of products and customers. It allows you to analyse performance and to model complex new scenarios for costs, prices and volumes. Managers can quickly see the effect of a radical refocusing of product portfolios and service offerings. It provides an authoritative basis for challenging their instincts and prejudices, and for supporting difficult decisions.

The analysis can often reveal:
- products and services that are failing to make sufficient contribution
- the need to raise prices to speed up withdrawal from a range
- the chance to increase selling prices, particularly of products strategic to customers
- special products and services with under-estimated overheads, which are not reflected in the price
- secondary products and services that should be subcontracted
- opportunities to cut costs selectively without jeopardising investment in the elements that are doing well.

When products are cut, it is essential to reduce the fixed costs that support them too. Other routes to low costs are:
- to focus on core competences – with better productivity rates
- to simplify procurement, handling, skills and complexity
- to improve efficiency and utilisation.

Product costing in manufacturing has been notoriously weak. Many firms have treated a product cost as a version of the direct cost (labour, materials, direct process overhead). Overhead has often been charged out on the basis of a percentage of direct labour, or direct material, or even sales value. This clearly works, on average! But it invariably under-costs low-volume, complex products at the expense of high-volume, simple ones. The high-volume products then become over-priced and uncompetitive – and fall in volume. Meanwhile, the business becomes overwhelmed with orders for the low-volume specials that are even more under-priced. The consequences are inevitable.

“Willingness to change is a strength, even if it means plunging part of the company into total confusion for a while.”

Jack Welch
Activity-based costing

Activity-based costing sets out to tackle this. It removes the concept of fixed/indirect costs and in practice makes all costs variable. Then all the costs and overheads of the resources used by each activity can be apportioned to it. So it becomes possible to evaluate the benefits and costs of changes in the organisation and activities.

Though simple in concept, activity-based costing can prove difficult in practice. How much detail is it worth investigating to justify the outcome? Too many data and a large product range will demand an army of analysts and a complex costing model that needs constant maintenance. Too few, and the result will be little better than a conventional costing system. Although it is possible to run activity-based costs monthly, the extra work is not usually justified. But periodic and one-off investigations to reset the base-line can be invaluable.

Equivalent units are an alternative way of evaluating the costs of products by:

- establishing the relative total conversion costs of all the products made in a single facility
- showing the impact on cost of changes in the product mix
- giving managers a way of measuring absolute changes in productivity over a long time
- encouraging a fundamental change in the attitude of managers and shop-floor employees to improving long-term productivity.

Total unit conversion costs are established for each product: this excludes materials. The total unit conversion cost of the product with the highest annual volume is set at one ‘equivalent unit’ and all other products are given relative ‘equivalent unit’ values. At the outset, the total annual costs of all the output will equate to the total conversion costs included in the equivalent units. From this point these equivalent unit costs are used to measure the total value of output.

As time goes by and the mix of products changes, the new volumes are calculated from the equivalent units to establish an output conversion value. This can be compared with the actual cost for any given period. If the actual cost is lower than the equivalent value of the output, then the productivity in unit conversion costs has improved.

The methodology is also used for budgeting, to encourage discussion of changes in productivity and investment. New products can be introduced at the original equivalent unit value. Ultimately, there will be both a historical equivalent unit cost and a current equivalent unit rate, the difference reflecting real improvements in conversion cost or productivity.

“The most important thing in communication is to hear what isn't being said.”

Peter Drucker
Marketing position and competitiveness

Success can be measured in many ways — such as profitability, growth in sales, market penetration, or return on capital employed. But any of these indicators may obscure what is really going on. Complacency soon sets in. The most profitable firms may be the least likely to consider change. They may fail to stay close to their markets and to find out — and act on — how their close customers see them.

Understanding customers better

When ‘the customer’ is a big firm, ‘its’ perceptions are not those of one person. The directors, the managers, the supervisors, and various workers who specify, procure, manufacture, distribute, use and maybe dispose of the product will influence the buying decision. So it is important to get the views of the wide range of people. It is helpful to build up an informal model of how the customers’ needs are actually fulfilled in practice. Such close analysis may help:

■ to gain greater respect from the senior managers of the customer, because you listen
■ to find out who the main competitors are — they may not even be in ‘this market’
■ to learn what really works and how the products and services are used in practice. This can highlight opportunities for improvement or differentiation
■ to provide a benchmark against which to measure future performance.

None of these can be gained from a simple questionnaire or telephone discussion. There is a clear return on the investment in a focused survey of selected customers. This knowledge can be a critical determinant of whether the required return on the investment will be achieved.

In analysing competitors, be clear what market and segments are being considered. Assiduous desk and telephone research can be supplemented by information from independent sources. But it pays to be wary of assessments of market share that all spring from a single, sometimes poor, piece of published research. Executives are less and less keen to be interviewed for research purposes. So it is worth working out how to reward them for their co-operation. And it can be useful for a group of companies to ask an independent researcher to analyse them all and to present the findings without naming names.

“I don’t want yes men around me. I want everyone to tell the truth, even if it costs them their jobs.”

Sam Goldwyn
Evaluating customer service

The real costs of service can be hidden in the total overheads. Yet meeting customers’ needs in different ways can double or halve net profit margins. Activity-based costing, as we have shown earlier, provides a mechanism to evaluate the actual costs of the business processes and the opportunity to review the consequences of serving customers in different ways.

Professor Michael Porter has presented a useful way to illustrate the conceptual relationship between competitiveness, value, and the costs of serving customers. The graph indicates that the willingness to accept an increase in cost rises and falls with the customer’s perception of value. At one extreme (A), increasing the cost of the service will have no impact on the customer’s perception of value. At the other (B), there is no saving in costs even though the customer’s perception of value declines. In between these two extremes, there is an infinite number of points where adding more cost will improve the customer’s perception.

However, within this theoretical curve, which Porter calls the ‘frontier of competitiveness,’ the unit cost exceeds the perceived value, making the supplier uncompetitive. It is then necessary to raise the perceived value faster than the unit cost.

In practice, total unit costs can be calculated, but perceived value can only be estimated or judged. Nevertheless, it is a helpful construct when considering the costs of changing service levels.

Pricing for competitive advantage

Pricing has become more sophisticated. Yet the failure of so many pricing structures is still evident. The management of customers’ perceptions can be more important than the price itself.

When a product or service has become undifferentiated, most purchasers know the price at which it should be traded. Therefore, any seller has to set the price at the competitive rate for the location and the speed/quality of service and delivery. If the expense of the operation means that this is not profitable, then the costs have to be reduced or the market abandoned.

Fortunately, market knowledge is often partial. So, for more differentiated items, there is scope to price on the basis of the nature of the customer; the frequency of demand; the scarcity of alternative suppliers and the service demanded. It is valuable to test the market from time to time by trying out new pricing policies on part of a range or selected groups of customers to minimise the risk and optimise the opportunity to learn.

The quickest way to raise the profitability of an operation is to review its pricing – and discounting – policy. It is common to find profit centres that set the price according to a catalogue or price list but allow excessive freedom to apply discounts, which can wreck profitability. The customers who apply the most pressure get the best discounts, no matter how much they buy.

Appraising the total cost of purchasing

The aggressive buyer driven by price (at all costs!) is a common source of fear and respect. However, the best price very often does not lead to the lowest overall cost.

An ambitious buyer of aluminium was keen to drive down the unit price by accepting delivery of a year’s supply. The business had the warehouse space to do this. But nobody had told the buyer that the specification was about to change, or that this particular aluminium ‘goes off’. The consequences were dire. However, more modest problems are commonplace. Part of the problem is the lack of communications about strategy and plans for fear that buyers will not use the information appropriately. Some purchasing professionals are unwilling to get out of their offices to learn how their principal purchases are used in practice.

A business absolutely devoted to service will have only one worry about profits. They will be embarrassingly large.”

Henry Ford

“Frontier of competitiveness

*Raise value and hold unit cost*

*Raise value and reduce unit cost*

*Hold value and reduce cost*

*Actual unit cost to deliver the product and service*
Managing in European markets

Managers need to make decisions about which markets to compete in; what type and range of products/services to offer; how to organise marketing and selling; and how to respond to competitors’ moves – whether these are from local, pan-European or world-wide operators. There are choices to be made about location, organisation, resources, people, processes and controls. Consumers, economics and politics are driving European markets to converge. Yet lots of national and regional idiosyncrasies remain. There is a balance to be achieved between ‘thinking regionally and acting locally’. A model ‘integrated’ organisation might include the features below:

Some sectors are already served by pan-European businesses. Others are defined by national or regional boundaries or have a more discrete specification. Though some consumer markets may seem to be converging, business-to-business sectors in many countries still have some traditional patterns. The challenge for pan-European businesses is to be able to meet the conflicting demands for standardisation and common products and for differentiation and regional specialisation.

Definitions of market share have been re-thought. Many large companies have previously dominated a national market with nominal ‘export’ sales. This becomes irrelevant if a French or Italian competitor is already gaining advantage by operating efficiently across several borders. Consolidation forces managers to consider carefully which markets they operate in and helps them to define their core business. Peripheral and less profitable products, services and customers can be jettisoned. This focuses operations on larger, clearly-defined sectors that can eclipse traditional, and now largely superficial, frontiers. It is the first step away from marketing that primarily builds on a series of separate national units.

Some local and national markets will remain important in their own right. They will be the source of advantage and innovation, or include the most discerning (or profitable) customers. Pan-European companies need to secure a larger share in a larger market but also to decide how they should compete in specific national segments.
This plaintive cry is not exceptional. The advent of the ‘global market,’ the Internet and web auctions has, as never before, piled the pressure on purchase prices. And yet the profitability of many international businesses has never been so buoyant. So what is happening?

One important factor is price-lag. There is a period between input prices falling and customers demanding price reductions. This effect is particularly marked when a new source of supply is introduced. There are set-up costs of the changeover and the value of goods in the pipeline that conveniently hide the real savings in inputs. Purchasing contracts can also be some protection on margins. But, in due course, customers cotton on to the opportunity to renegotiate prices.

Increasing use of suppliers in South East Asia and Eastern Europe is highlighting the trade-off between direct labour costs and lead-times for supply. Increasingly sophisticated industrial and technological capacity in these regions is allowing indigenous businesses to compete with the best in labour and capital investment. Printers, for example, in Eastern Europe can provide tough competition to those in the rest of the European Union because they have relatively low labour costs but also high capital investment. Instability in currency markets reinforces the importance of flexible modelling that can work through ‘what-ifs’ easily and accurately.

The economics of global supply chains need careful modelling if the true costs and benefits are to be evaluated. It is possible to create a basic economic model of costs and throughputs to optimize the use of capacity in different parts of the world. Local managers often need help to gather, analyse and present comparable information.

Global sourcing

“All I have achieved by outsourcing my manufacturing to China is that I have reduced my average sales value and passed on all the benefit to my customers in reduced financial margin!”

Chief Executive of a large multinational.
One such investigation of the technical capabilities, capacities and demand of a manufacturer resulted in the extraordinary finding that supply chain costs could be reduced significantly while capacity was actually increased by the same proportion. A small part of this model is illustrated in the diagram.

The complexity of such a model needs to be sufficient to represent fairly what is happening in practice without burying the investigation in unmanageable data. The collection and analysis of the information that drives the model demand careful thought and testing before a world-wide hunt for information is initiated. Data on cost and capacity are notoriously inaccurate and inconsistent between operations and countries. A data dictionary for definitions and rules for analysis are essential if information from various accounting jurisdictions is to be comparable. Even then, conclusions need to be tentative until verified in practice. The process of investigating the economics of alternative scenarios is worthwhile for its own sake.

Value analysis and value engineering provide powerful tools for getting behind the cost structure of products and the underlying costs of conversion. In a highly competitive market, survival may depend on squeezing 10% of the cost out of an already mature product. Close liaison with the purchasing function can bring great benefits.

“He that will not apply new remedies must expect new evils; for time is the greatest innovator.”

Francis Bacon
Relocating sites and operations

Relocating a business unit is complicated. But while it is in progress, the business must continue to perform. The risks are considerable. The cost and schedule may overrun; and skilled managers may be diverted from their everyday tasks.

Should a business share overheads and services by combining sites? The core question concerns the perceptions of customers. Even manufacturing sites that have no facility for serving customers can have a marketing purpose, as a visible commercial presence. Closing a distribution or sales outlet can have a significant impact on sales in that area or region. However well a supplier is respected, its location is crucial.

Customers balance cost and convenience. An item may be cheaper in the next town. But a local supplier is much handier.

Closure – an opportunity

Even a closure that is necessary and worthwhile can pose a threat to the business. And yet, during a well managed closure, performance may actually increase. To that end:

- justify the case for closure – profitable sites are difficult to close
- manage communications and consultation carefully
- administer the procedures scrupulously – in both the spirit and the letter
- maintain good relationships with local officials and politicians
- form relationships with local businesses that may be able to absorb some of the employees
- help people to find new jobs or to be retrained
- offer a relatively generous deal. It helps to give an incentive to the employees who stay to the closure date and achieve the required output, quality and service.

A closure should be managed as an opportunity to establish new ways of working at the host site and to leave behind a sense that the company did everything it could to mitigate circumstances beyond its control.

The European dimension

To close a site in the United Kingdom is never straightforward. However, it is usually easier than in mainland Europe, where managers usually need to draw up a social plan acceptable to the workforce as well as to local government officials. The social plan sets out how all the employees are to be treated in their individual and personal circumstances. In some cases, a complex procedure has to be followed to the letter and to a strict schedule over many months. Any minor infringement in process, schedule or communication can mean the whole programme has to start all over again. And if the closure of a site in a small town becomes a ‘cause célèbre’ that the local politicians can get their teeth into, fur may fly. Acrimony, protests, sit-ins: all Hell can be let loose.

So the period of closure needs firm and stable general management with a project manager leading the closure while the general manager concentrates on keeping the business going.

Managing excess European capacity

A leading manufacturer of paper products reviewed its capacity in Western Europe and decided to consolidate production on fewer sites. So a long-established mill in southern France was declared redundant. Collinson Grant planned the closure without disrupting production, at least cost, and in full compliance with complex French employment law. Overall capacity was maintained by increasing production at the Belgian factory. An interim general manager ran the French factory for ten months and maintained its output. Meanwhile, consultants led sensitive negotiations with the unions, local political leaders and government officers. A Social Plan, which reduced the company’s legal and financial exposure, was drafted and accepted. Considerable local opposition to the closure manifested itself in scurrilous publicity, lock-ins and more intimidating measures. But the factory was closed two months ahead of schedule.

The company’s British managers had underestimated the complexity of French legal requirements in restructuring, and the potential associated costs. They were relieved that we were able to realise the plan and round off the closure without serious hindrance. In the event, the local officials were grateful for the way in which the closure had been handled.
Restructuring multinational businesses

Businesses that span countries and continents can have very different structures:

- **local (national or regional) commercial operations but centralised production and services**
- **several manufacturing units in different countries, located to exploit cheaper labour and resources**
- **dispersed profit centres, united only by common ownership and branding**
- **a selling model and supply chain that use internet-based technologies for speed and reach.**

In each case, the demands on the organisation and its managers are different. So fresh thinking is required on the necessary operating processes and managerial controls. There is a trade-off between the stability of established economies in which a business has been competing for years and the challenges of new markets with prospects for growth and lower costs.

The true pan-European company transcends regional and national boundaries and is structured to operate as a single entity. It is likely to be focused on one clearly defined market and to comprise:

- a single structure, usually with no country-by-country spans of control
- centres of excellence in production and services
- shared services
- consistent managerial controls and reporting of performance
- unified supply processes
- common ways of managing and rewarding people.

Although few companies will aspire to such an ‘idealised’ model, many businesses have adopted several of these features and then tailored them to their exact circumstances and history. Continued convergence of markets and consolidation in many sectors is forcing many to examine the rationale of their current model.

**Restructuring options**

During the restructuring of a multinational firm, different questions will arise. How is the company managed? Where are the key functions located? How can effective communication be maintained?

- What are the implications for recruitment, reward and retention of creating a fully international managerial team?
- How much investment will be required?
- Should the Group’s headquarters be relocated to reflect the natural locus of the business?
- What is the most common language used in the Group and should this become the ‘standard’ for internal communications?

- How many of the acquiring company’s policies and working practices should be amended to take account of good practice in an acquired business?

Many companies have sought to move some of their operations to mainland Europe, conscious that they run the risk of becoming less competitive as the global economy expands. Because labour laws are restrictive in many western European countries, this is often seen as a substantial challenge. It need not be, if:

- the objectives are clear
- the legislation and process are properly understood
- a budget is set which has a realistic assessment of likely costs and necessary contingencies
- adequate time is built into the implementation plan for the required consultation and negotiation
- specialist advice is obtained at the right time.

Making redundancies – in France and Germany, for example – is not easy. But it can be achieved without damaging the business, if care is taken at every stage.

**Employment practices in European businesses**

Companies with European structures have often learned the hard way that national labour markets usually have more differences than similarities and that managing people in different countries is not straightforward.

Some labour markets are highly regulated at regional and/or national levels. There are significant pay differentials, especially between northern and southern European states. And the ways in which employers and employees negotiate and resolve disputes vary considerably. Despite all this, a pan-European business should have, as far as is practicable, consistent employment policies and practices throughout.

How far these can be translated into common procedures and the full harmonisation of European terms and conditions depends on specific, local circumstances.
Constructive employee relations

Restructuring should aim to promote new and constructive employee relations. But that takes time, patience, and a consistent approach.

The management of employee relations has, thankfully, moved on from the set-piece battles over the annual pay review. The justification for higher pay should be increased productivity. But that can be hard to measure over a long period in a way that both sides see as fair.

There is a temptation to start by conducting attitude surveys and personal appraisals on ‘soft’ issues such as ‘culture and values’. And they have their place. But they will be ineffective until the infrastructure of employee relations has been set on a firm foundation of strong leadership, effective procedures and agreements, managerial resilience under challenge, clear processes for communication and consultation, and indicative, agreed, changes in operations.

<table>
<thead>
<tr>
<th>Strong leadership</th>
<th>Ineffective employee relations may be down to weak leadership, perhaps over many years. Employees like well known rules to be consistently applied. If managers and supervisors fail to do so, any strong character may emerge as the ‘daddy’. So the first thing to do is to appoint a competent and experienced General Manager.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Effective procedures and agreements</td>
<td>Well-documented procedures and agreements are essential. Without them, attendance may well be poor, product/service quality inadequate, housekeeping neglected, training undervalued and health and safety requirements paid only lip-service. The creation of a new set of procedures gives the managers and the staff a chance to discuss and to agree on the challenges facing the business. Some disciplinary procedures may, in the end, have to be imposed. But comfort should be taken from experience. Each procedure that is established paves the way for the next one.</td>
</tr>
<tr>
<td>Managerial resilience under challenge</td>
<td>If there has been a long period of neglect, it is inevitable that a few people, maybe of disproportionate influence, will not respond constructively to the change in regime. So the managers must take a tough line with them. Monitoring their attendance, performance, adherence to health and safety rules, and discipline will pay off in the end. Confrontation should be a last resort. But it may well be necessary if protracted discussion and consultation are unsuccessful. Take particular care to apply disciplinary procedures consistently. Otherwise all the good work done over the months and years can be undermined in days.</td>
</tr>
<tr>
<td>Clear processes for communication and consultation</td>
<td>Establish straightforward methods of communication between managers and employees straight away. There are many opportunities for misunderstanding early on when there is little mutual respect, but these can be overcome by careful and consistent communication. Processes for consultation will first require effective mechanisms for communication. The structures for consultation should reflect the nature of the business, the geography and independence of sites, unionisation and the requirements of employment law.</td>
</tr>
<tr>
<td>Indicative, agreed, changes in operations</td>
<td>Set up one or two ‘working groups’ with managers and employees to discuss and make pressing practical changes that, if successful, can provide early gains. Working together to make beneficial change encourages employees to see the positive side to discipline and procedures. Most employees respond to rewards for good attendance, excellent work, and involvement in improving the workplace, and are glad to see the back of the old practices.</td>
</tr>
</tbody>
</table>
Once again, clear accountabilities, managers who are confident in what they are doing, and efficient processes promote a healthy business and a productive, contented workforce. So a large part of the effort in restructuring is concentrated here.

**“The magic formula that successful businesses have discovered is to treat customers like guests and employees like people.”**

**Tom Peters**

**Tackling long-standing problems**

People represent the biggest single cost, and their main motivation is pay. So the terms on which they are employed are critical to the success of the business. Due diligence should have revealed obvious inconsistencies and scope for improvement. Sometimes the business case for integration or restructuring will be based on a more cost-effective structure and on linking reward to performance better. Changes to the ‘employment package’ are usually difficult to implement. They take time. But this is not a reason for missing the opportunity.

**Terms and conditions of employment** – new circumstances (changes in hours, the content of jobs and location) may demand a review of terms and conditions. But these form a contract and can only be changed by mutual agreement. So take care. The objective should be consistency, simplicity and a degree of flexibility. A contract is not for review every day but should form a reliable basis of trust and should sustain confidence in a continuing relationship. It should reflect reality, not aspiration.

**Pay structure** – nearly all pay structures get distorted over time and no longer serve the true aims of the business. Managers make exceptions to rules without enough justification, or ignore the structure when it serves their purpose. Most tinkering results in higher rather than lower pay, so the result is a serious drain on profit. Restructuring provides a rationale for re-examining pay structures, and the chance to link pay to performance. Better measures and controls throughout the business will determine where it is possible and sensible to create performance-related rewards and how they should work. Careful maintenance of reward structures is essential – as circumstances change they can rapidly become ineffectual.

The outcome should be a satisfactory balance between the expectations of shareholders and employees:

**Employee relations** – the receptiveness of employees to change suggests the state of employee relations – but nearly everybody will have some reservations. Trades unions need to be engaged as early and as openly as possible. Good union leaders can be powerful allies when they understand fully the reasons for change and see some advantage for their members. Some degree of mistrust in negotiations is almost inevitable, but it should be countered by consistency and transparency.

**Managing performance** – there should be no doubt how the business is to be managed and where responsibility for financial control and profit will reside. The new culture should emphasise excellent performance throughout the business with:

- consistent and well-publicised values and behaviours
- well-designed performance management processes
- visible, early and substantive actions.

Statements on new values typically will highlight the importance of customers, employees, other partners, high performance and innovation. They should set out clearly what needs to be done to realise the company’s aspirations.

A sophisticated process for managing performance is required to get better results from people. Performance management provides that agreed objectives and requirements for skills, competence and training are continually reviewed to improve learning, development and motivation. Managers need to discuss with the employees their inputs and outputs, their agreed roles, and their contribution to the performance of the team.

**Managerial capability** – it is not uncommon for there to be a crisis in the supply of experienced managers. Succession planning and management development may have been neglected, leaving little new talent in the pipeline. The age profile of the current cadre may be dangerously skewed. A number of approaches can be used to assess managers’ skills and potential. The options that we use include:

- individual assessment – using structured interviews, personality assessment and cognitive tests, to provide quantitative and qualitative data
- group administration of personality assessments and cognitive tests, yielding comparative data
- an assessment centre for small groups, comprising behavioural exercises, personality assessment, cognitive tests and group inter-action.
It is feasible for the senior line manager to have this accountability, but that will depend on the strength of the management team and the nature of the proposed changes. A programme manager does more than manage a specific series of projects. She or he has to have a sound understanding of how the whole programme will bring about a sustained improvement in trading performance and profitability.

The programme manager should:

■ know the business well and understand its culture
■ have strong interpersonal skills and the credibility to be able to intervene quickly when the situation demands, and
■ have a reputation as somebody who gets things done.

The main tasks of a programme manager should be:

■ to confirm the overall strategy for change
■ to plan the total programme, organise the staff and provide appropriate training and briefing
■ to establish and own the processes for managing projects and restructuring
■ to control communication and ensure that consistent and positive messages reach all parts of the business through formal and informal channels
■ to co-ordinate and facilitate change in close liaison with the senior line manager responsible for the programme and its success
■ to monitor the close integration of the change programme with the plans for the trading business – and consequently
■ to assess the risks inherent in taking action and ensure that projected performance is not jeopardised. This inevitably entails balancing pragmatic, short-term action with the longer-term plans for change.

A framework for programme management is illustrated in the diagram:
It is also important:

■ to apply rigorous control to the project management process, ensuring, in particular, that projects do not pass ‘gates’ without approval from a lead body, such as a Steering Group
■ to facilitate the adequate manning of project teams by getting senior managers to release their full-time or part-time members from other work
■ to conduct formal reviews of progress at agreed intervals and provide the lead body with suitable progress reports
■ to review the processes of project management, promote their adoption as good practice throughout the body and create mechanisms to assess how well they support the aims of the programme
■ to establish, with line managers, resources, processes, values and attitudes that will sustain the outcomes of projects
■ to create and manage a process for the formal evaluation of each project and the overall change programme.

“As the births of all creatures are at first ill-shapen, so are all innovations, which are the births of time.”

Francis Bacon

The formal processes of project management need to be supplemented by the behavioural framework of change management, which focuses on the necessary knowledge, skills and attitudes. Programme managers need to take action to instil the ability to react more quickly to competitive forces and initiate tactical improvements without recourse to formal projects and external support. This is shown in the diagram:

Understanding the culture

An ability to recognise quickly and precisely the influences and forces at work, and to respond to them, greatly enhances the chances of effective progress. It can be useful to conduct a ‘cultural’ audit at each site and to review the results carefully before planning any major change. A series of short, questionnaire-based surveys may be used to provide a snapshot of the firm and its readiness for change. These are reinforced by structured interviews with selected managers. The results provide an objective benchmark against which to measure progress. For example:

<table>
<thead>
<tr>
<th>Cultural dimensions</th>
<th>Strongly agree</th>
<th>Agree</th>
<th>Neither agree nor disagree</th>
<th>Disagree</th>
<th>Strongly disagree</th>
</tr>
</thead>
<tbody>
<tr>
<td>Top management encourage and support new ideas</td>
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<td></td>
<td></td>
</tr>
<tr>
<td>I am proud to work for this company</td>
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<td></td>
<td></td>
</tr>
<tr>
<td>The pressures and difficulties of my job do not allow me to take pride in my work</td>
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</tr>
<tr>
<td>It is easy in this company to admit to a mistake</td>
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</tr>
<tr>
<td>Creative people are given every encouragement</td>
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<td></td>
<td></td>
</tr>
<tr>
<td>My manager is too busy to think creatively</td>
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<td></td>
<td></td>
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<tr>
<td>I enjoy my work</td>
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<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>There is a good spirit in this company</td>
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</tbody>
</table>
Such tools must be used sparingly. They raise expectations that subsequent actions will be swift and decisive. If they aren’t, the confidence that the workforce places in its managers is lost. And it is not easily regained. Unless adequate time is built into plans to surmount these hurdles systematically, the costs of major restructuring will increase and the benefits will be realised much more slowly than expected.

Establishing the case for change

All organisations are subject to constant, minor change. But for major change a clear, compelling business case must be made and proven. It should marshal quantitative and qualitative arguments to generate a sense of urgency in senior managers. The new objectives that result will support the development of a fresh vision and plan for the business. Managers are most committed to ambitious programmes of change for which they have analysed and defined the need.

Formulating a vision and a strategy

A vision of where the business will be, what it will look like and how it should behave in the future should be derived from the case for change. This should be formulated in a series of short, unambiguous statements that set out clearly what has to be achieved and by when. A vision is no use without a route-map to it. This should set out the main business arguments and competitive reasoning that justify a programme of major change.

Building the team and supporting infrastructure

The infrastructure for managing change should be defined to meet the circumstances of each case. Led by a programme manager, it should balance the influence of a steering group (representing the sponsor), the managers and staff from the business units themselves, the project teams and the specialist advisers.

The project teams should be the principal agents of change. They should comprise people with a mix of technical abilities and personal styles, not necessarily all senior, but respected by their peers, and not outsiders. The business needs ‘movers and shakers’ whose commitment is not in doubt, tempered with a few known cynics. Many businesses use project teams as a valuable testing ground for managers.

Champions can instil a sense of urgency and a spirit of ‘can do’. They should be found at an early stage, trained when appropriate and used to promote the messages for change and to cascade the programme throughout the business.

Planning for change

A rigorous programme for managing change is driven by a comprehensive project plan that integrates hard and soft elements. Each becomes a catalyst for the other, but only when they are managed in parallel. This is illustrated opposite:

<table>
<thead>
<tr>
<th>Examples of ‘Hard’ changes</th>
<th>Examples of ‘Soft’ changes</th>
</tr>
</thead>
<tbody>
<tr>
<td>Introduce a new invoicing system</td>
<td>Revise the techniques for credit control</td>
</tr>
<tr>
<td>Reduce the staff</td>
<td>and improve negotiating skills</td>
</tr>
<tr>
<td>Restructure the organisation</td>
<td>Motivate the survivors</td>
</tr>
<tr>
<td>Change processes for serving customers</td>
<td>Offer new terms and conditions and rewards</td>
</tr>
<tr>
<td>Revise the management information systems</td>
<td>Change managerial accountabilities and behaviours</td>
</tr>
<tr>
<td></td>
<td>Train the staff to deal with customers</td>
</tr>
<tr>
<td></td>
<td>Get managers to change their behaviour</td>
</tr>
<tr>
<td></td>
<td>and apply new skills</td>
</tr>
</tbody>
</table>

Communication and consultation

A carefully drafted plan for communication should be an integral part of every programme of change. This should be a two-way process. It is vital to elicit opinions and to listen to employees’ fears and concerns. It is useless to foist information on an audience that might not want to listen. At different stages, managers should check the employees’ reaction to change, and their commitment to the new working practices. This can be achieved through paper or web-based surveys, focus groups and/or structured and semi-structured interviews. A continuous stream of informed responses makes it possible to refine and adapt the change programme to enhance its prospects of success.

Communication is a sophisticated process. Its planning must match its execution. The key messages should be in line with the published strategy, consistent, honest, and reiterated. It is vital to set up and manage communication between different change teams, as well as with programme managers and employees.
Managerial competences

Every manager should be able to manage change. But some do it better than others. The culture provides the framework for honing skills. But a major project offers the chance to assess gaps and add competences. This is horses for courses. Depending on the circumstances, a manager may have to show the ability to lead, to negotiate political minefields, to build teams, to use a range of analytical techniques, or to meet testing circumstances with energy and commitment.

Putting the new structure in place

This can be set up, in stages if necessary, when each of the previous steps has been taken. The project plan will determine, for each package of work, what it will cover, how long it will take, how it should fit in with other work, and who is responsible for doing it. Its components might be:

- a new organisational chart with revised managerial accountabilities and staffing
- flow-charts to show the key business processes and sub-processes
- a description of the impact of changes in the structure and business processes on relationships with customers and/or suppliers and with any other parties affected
- a description of the main effect of the changes on employees, including any necessary changes to terms and conditions of employment and reward
- an assessment of the principal risks in the proposed change and the actions necessary to mitigate them
- a summary of the expected benefits and when they should be realised.

Achieving early results

Success breeds success. So it is useful to make tangible gains early on in the programme. This reinforces the commitment of all, wins over the doubters and keeps the approval of the sponsors. The opportunity for quick wins should be built into the project plan – so they should not be unexpected. They should provide mechanisms for testing new ways of working that provide confidence that larger initiatives in the pipeline can be realised satisfactorily. Early success should be celebrated and communicated widely throughout the organisation.

Monitoring and review

Every significant programme of change should have formal processes for monitoring and review. These should normally be an integral part of the project plan. They ensure that the programme maintains its momentum and provides benefits when and where they have been planned. And they record data and experiences that can contribute to the success of future initiatives.

Managing redundancy

Redundancies should be conducted fairly. This fulfils legal requirements and moral commitments to loyal employees. It helps to protect a reputation as a caring employer. And it sends a signal to the survivors – on whom the business now relies heavily – that everything is being done to help the redundant employees through a difficult time. This is most important. Insensitivity can colour the views even of people not directly affected by it.

Summary

There is no one right way to restructure. The approach depends on the aims and circumstances. The topics set out in this document are all ones that might need to be considered in a large-scale restructuring of a complex business. Often managers will not have the full range of skills and experience to conduct such an exercise – but being responsible for a major programme of change is an excellent proving ground. With the right support and leadership they can emerge as much better all-rounders, equipped to become senior executives in the new organisation.

As in most situations, success in restructuring depends on a few critical factors:

- thorough planning – but retaining the ability to adapt targets to changing circumstances
- sound decision-making – based on reliable data and robust analysis
- strong leadership – with a ‘can do’ attitude
- clear focus – on improving performance, and on day-to-day results
- determined implementation – using the formal techniques of programme management
- effective communications – particularly with those most affected by change
- good luck!

Collinson Grant

Collinson Grant is a management consultancy with a history of profitable growth. We help large organisations all over Europe and in the United States to restructure, merge acquisitions, cut costs, increase performance and profit, and manage people. We build long-term relationships, and have worked for some clients for over thirty years.

Our emphasis is on implementation, results and value-for-money. We expect to give a substantial return on the investment in us. So we do not recommend action unless we are sure that the outcome will be worth it. We are not afraid to give bad news, or to champion ideas that may not be welcome.

Most of our work is on three themes – organisation, costs and people. We use this simple framework to manage complex assignments – often with an international dimension – and to support managers on smaller, more focused projects.

We help them:

- to restructure and integrate – following acquisitions or to improve profits
- to improve the supply chain. We examine every process and interface to improve efficiency and service
- to set up financial and managerial controls. We create robust systems to improve decision-making and reduce risks
- to refine business processes and introduce lean manufacturing. We analyse and improve how work is done, and use new ways to create change and make it stick
- to cut costs. We make systematic analyses of overheads, direct costs, and the profitability of customers and products. This helps managers to understand complexity, and to take firm steps to reduce it
- to manage people. We draw up pay schemes and put them into effect, guide managers on employee relations and employment law, get better performance from people, and manage redundancy.