D.N.R.COLLEGE, (AUTONOMOUS): BHIMAVARAM
DEPARTMENT OF MANAGEMENT STUDIES

VUCA MANAGEMENT

III SEMESTER

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CP - 302, VUCA MANAGEMENT
MBA III SEMESTER eNOTES

UNIT – II: Industrial sickness –Causes, Consequences – Crisis Management – Types of Crisis & Turnaround Strategies.

Industrial Sickness

Industrial sickness refers to the uneconomical performance of industrial entities. It reflects poor functioning of business operations and suggests that something has seriously gone wrong with the usual business running.

As the term indicates, industrial sickness is related with industrial/ production/ manufacturing units of large, medium and small scale businesses. Similar to the sickness of human body, industrial sickness also has its own causes, symptoms, consequences as well as remedies.

Definition

According to Companies (2nd Amendment) Act, 2002:

"Sick Industrial Company" means an unit which has accumulated losses in any financial year which are equal to 50% or more of its average net worth during 4 years immediately preceding such financial years or Failed to repay its debts within any 3 consecutive quarters on demand made in writing for its repayment by a creditor or creditors of such company.

Symptoms of Industrial Sickness

1) Inappropriate utilization of resources.
2) Rejection rate of goods manufactured is very high.
3) Overuse of cash credit facilities on a regular basis and failing to pay instalment on credits and interest on loans taken from banks and other financial institutions
4) Constant inconsistency prevailing in cash, credit accounts.
5) Failure to pay statutory liabilities.
6) Employing working capital funds for financing capital expenditure
7) Continuous loss of profits, fluctuations or downward trends in sales and stagnation followed by downfall in the market share.
8) Longer and larger outstanding bills.
9) Diverging industrial funds and employing it to other purposes which may not relate to industry.
10) A major decline in the market causing failure of all the units engaged in this industry.
11) Conducting quick expansion activities and too much diversification with a short interval of time.
12) Several law suits pending against the firm.
13) Frequent changes made in the management of the industry including professional or an individual authority.
14) Failure to submit periodical financial data, stock statement, etc.

Internal Causes for Industrial Sickness

1) Lack of Finance:

Lack of finance is one of the internal disorders which may lead to industrial sickness. It may be caused due to insufficient funds involving uneconomical and unproductive working capital management, improper utilization or diversion of funds, weak equity base, exclusion of planning and budgeting, deficient use of assets and use of inappropriate costing and pricing methods.

2) Bad Production Policies:

The next reason for sickness can be related to the production decisions viz. choosing inefficient site for conducting production activities, poor maintenance of plants and machineries, absence of quality control measures, absence of standard research and development techniques, etc.

3) Marketing and Sickness:

The health and vigour of an industry is invariably influenced by its marketing activities. An inappropriate marketing strategy may cause poor performance of its products and services in market, and ultimately lead towards industrial sickness.

4) Inappropriate Personnel Management:

Improper personnel management yet another cause for sickness of an industry. Lack of efficient personnel management policies can be observed in the form of mismanagement of wages and salaries of employees, absence of behavioural approach causing discontentment and resentment among workers and employees, inefficient labour relations, etc.

5) Ineffective Corporate Management:

Another important internal cause for industrial sickness is ineffective corporate management. If the corporate policies are inappropriate, its top management lacks integrity and the control lacks among corporate managers and authorities, then such reasons become the major cause for industrial sickness.

External Causes for Industrial Sickness

These are the external factors which are beyond the control of management of an industry. Some of these external factors are as follows:

1) Personnel Constraints:

Personnel constraints such as lack of availability of skilled manpower or labour, disparity in wages of employees and labours as compared to other industries, and the type of labour employed/available in a region.

2) Marketing Constraints:

Marketing constraints include recession in market, liberal licensing and tax policies imposed by the government and regulation on making bulk purchases, dynamic international market environment which may undergo sudden changes, etc.

3) Production Constraints:

Sickness of small scale industries also arises due to the lack of power supply, fuel and high prices, dearth of raw material, import/export restrictions, etc. These factors are categorized as product constraints causing industrial sickness.

4) Financial Constraints:

The last most common external cause of sickness in an industry is financial constraints. Such constraints may arise due to any delay in disbursement of loan by government, unfavourable investments etc.

Consequences of Industrial Sickness

1) Large-Scale Unemployment:
When a sick unit fails to take forward its operational activities and consequently shuts down, then the number of workers and labour engaged in such industries become unemployed.
Such consequence is severe if the industrial unit is employing large scale workforce

2) Wastage of Resources:
India being a capital deficient economy can encounter adverse effects, if an industrial unit is shut down due to sickness as all the resources invested in that unit will be wanted. This issue is especially critical for large scale sick units where considerable investments are employed in setting up of plants and machinery.

3) Adverse Effects on Related Units:
Forward and backward connections create a linkage between different industries. Due to this reason, failure of one industry is expected to affect the other related industries as well. For example, a textile unit which purchases its raw materials and other inputs from other industrial unit and sells the manufactured products to other. Therefore, if the textile unit becomes sick, it will possibly influence the business operations of these associated industrial

units.

4) Industrial Unrest:

The closure of a large-scale industrial unit may lead to the rising unrest among the workforce engaged in such unit. Such unrest may cause situations of strike which will affect the overall industrial environment affecting the production of several other associated units.

5) Adverse Effects Investors and Entrepreneurs:

The investors who have invested their capital in an industrial unit may be largely discontented if such unit becomes sick and closes down. Such discontentment among the existing investors may also discourage the prospective investors willing to invest in these industrialunits.

6) Losses to Banks and Financial Institutions:

Banks and other financial institutions which have provided credit to sick industrial units suffer considerable financial losses on account of closure of such units. For example, ICICI, IDBI and IFCI have witnessed such losses due to the non-recovery of loans provided to the industrial units that are now categorized as sick units. Such large-scale losses may cause inadequacy of funds among banks and financial institutions arising due to blocked funds.

7) Decline in the Revenue of Government:

A huge amount of revenue is generated by the central, state and local governments from industrial units in the form of taxes and duties imposed on these units. Moreover, industrial sickness causes decrease in the amount of revenue generated by the government from these units.

MEANING OF CRISIS

A sudden and unexpected event leading to major unrest amongst the individuals at the workplace is called as organization crisis. In other words, crisis is defined as any emergency situation which disturbs the employees as well as leads to instability in the organization. Crisis affects an individual, group, organization or society on the whole.

Characteristics of Crisis

- Crisis is a sequence of sudden disturbing events harming the organization.
- Crisis generally arises on a short notice.
- Crisis triggers a feeling of fear and threat amongst the individuals.

Crisis can arise in an organization due to any of the following reasons:

1. Technological failure and Breakdown of machines lead to crisis. Problems in internet, corruption in the software, errors in passwords all result in crisis.
2. Crisis arises when employees do not agree to each other and fight amongst themselves. Crisis arises as a result of boycott, strikes for indefinite periods, disputes and soon.
3. Violence, thefts and terrorism at the workplace result in organization crisis.
4. Neglecting minor issues in the beginning can lead to major crisis and a situation of uncertainty at the work place. The management must have complete control on its employees and should not adopt a casual attitude at work.
5. Illegal behaviours such as accepting bribes, frauds, data or information tampering all lead to organization crisis.
6. Crisis arises when organization fails to pay its creditors and declares itself a bankrupt organization.

Crisis Management

The art of dealing with sudden and unexpected events which disturbs the employees, organization as well as external clients refers to Crisis Management.

The process of handling unexpected and sudden changes in organization culture is called as crisis management.

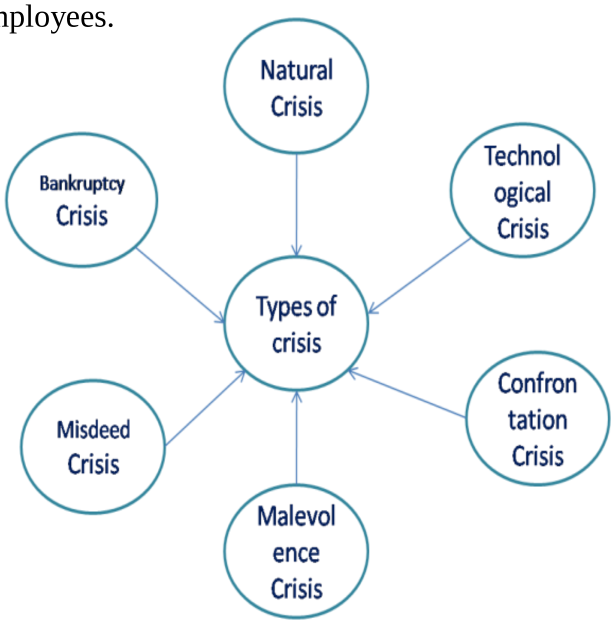
Need for Crisis Management

1. Crisis Management prepares the individuals to face unexpected developments and adverse conditions in the organization with courage and determination.
2. Employees adjust well to the sudden changes in the organization.
3. Employees can understand and analyze the causes of crisis and cope with it in the best possible way.
4. Crisis Management helps the managers to devise strategies to come out of uncertain conditions and also decide on the future course of action.
5. Crisis Management helps the managers to feel the early signs of crisis, warn the employees against the aftermaths and take necessary precautions for the same.

TYPES OF CRISIS

Crisis refers to sudden unplanned events which cause major disturbances in the organization and trigger a feeling of fear and threat amongst the employees.

Following are the types of crisis:



Natural Crisis

1. Disturbances in the environment and nature lead to natural crisis.
2. Such events are generally beyond the control of human beings.
3. Tornadoes, Earthquakes, Hurricanes, Landslides, Tsunamis, Flood, Drought all result in natural disaster.

Technological Crisis

1. Technological crisis arises as a result of failure in technology. Problems in the overall systems lead to technological crisis.
2. Breakdown of machine, corrupted software and so on give rise to technological crisis.

Confrontation Crisis

1. Confrontation crises arise when employees fight amongst themselves. Individuals do not agree to each other and eventually depend on non-productive acts like boycotts, strikes for indefinite periods and soon.
2. In such a type of crisis, employees disobey superiors; give them ultimatums and force them to accept their demands.
3. Internal disputes, ineffective communication and lack of coordination give rise to confrontation crisis

Malevolence Crisis

1. Organizations face crisis of malevolence when some notorious employees take the help of criminal activities and extreme steps to fulfil their demands.
2. Acts like kidnapping company's officials, false rumours all lead to crisis of malevolence.

Misdeeds Crisis

1. Crises of organizational misdeeds arise when management takes certain decisions knowing the harmful consequences of the same towards the stakeholders and external parties.
2. In such cases, superiors ignore the after effects of strategies and implement the same for quick results.

Crisis of organizational misdeeds can be further classified into following types:

Crisis of Skewed Management Values: Crisis of Skewed Management Values arises when management supports short term growth and ignores broader issues.

Crisis of Deception: Organizations face crisis of deception when management purposely tampers data and information. Management makes fake promises and wrong commitments to the customers. Communicating wrong information about the organization and products lead to crisis of deception.

Crisis of Management Misconduct: Organizations face crisis of management misconduct when management indulges in deliberate acts of illegality like accepting bribes, passing on confidential information and so on.

Crisis due to Workplace Violence: Such a type of crisis arises when employees are indulged in violent acts such as beating employees, superiors in the office premises itself.

Crisis Due to Rumours: Tarnish the Spreading false rumours about the organization and brand lead to crisis. Employees must not spread anything which would image of their organization.

Bankruptcy Crisis: A crisis also arises when organizations fail to pay its creditors and other parties. Lack of fund leads to crisis.

Natural Crisis: Disturbances in environment and nature such as hurricanes, volcanoes, storms, flood; droughts, earthquakes etc result in crisis.

Sudden Crisis: As the name suggests, such situations arise all of a sudden and on an extremely short notice. Managers do not get warning signals and such a situation is in most cases beyond any one's control.

Smoldering Crisis: Neglecting minor issues in the beginning lead to smoldering crisis later. Managers often can foresee crisis but they should not ignore the same and wait for someone else to take action. Warn the employees immediately to avoid such a situation.

CRISIS MANAGEMENT MODEL

Gonzalez-Herrero and Pratt proposed a Crisis Management Model which identified three different stages of crisis management.

According to Gonzalez-Herrero and Pratt, crisis management includes following three stages:

1. Diagnosis of Crisis

The first stage involves detecting the early indicators of crisis. It is for the leaders and managers to sense the warning signals of a crisis and prepare the employees to face the same with courage and determination. Superiors must review the performance of their subordinates from time to time to know what they are up to.

The role of a manager is not just to sit in closed cabins and shout on his subordinates. He must know what is happening around him. Monitoring the performance of the employee regularly helps the managers to foresee crisis and warn the employees against the negative consequences of the same. One should not ignore the alarming signals of crisis but take necessary actions to prevent it. Take initiative on your own. Don't wait for others.

2. Planning

Once a crisis is being detected, crisis management team must immediately jump into action. Ask the employees not to panic. Devise relevant strategies to avoid an emergency situation. Sit and discuss with the related members to come out with a solution which would work best at the times of crisis. It is essential to take quick decisions. One needs to be alert and most importantly patient. Make sure your facts and figures are correct. Don’t rely on mere guess works and assumptions. It will cost you later.

3. Adjusting to Changes

Employees must adjust well to new situations and changes for effective functioning of organization in near future. It is important to analyze the causes which led to a crisis at the workplace. Mistakes should not be repeated and new plans and processes must be incorporated in the system.

Turnaround Strategies:

A turnaround is the financial recovery of a company that has been performing poorly for an extended time. To affect a turnaround, a company must acknowledge and identify its problems, consider changes in management, and develop and implement a problem-solving strategy.

Following are certain **indicators** which make it mandatory for a firm to adopt this strategy for its survival. These are:

- Continuous losses
- Poor management
- Wrong corporate strategies
- Persistent negative cash flows
- High employee attrition rate
- Poor quality of functional management
- Declining market share
- Uncompetitive products and services

Also, the need for a turnaround strategy arises because of the changes in the external environment, change in the government policies, saturated demand for the product, a threat from the substitute products, changes in the tastes and preferences of the customers, etc.

Features of Turnaround Strategy

1. Turnaround involves restructuring the sick company.
2. It is applicable to a loss-making unit.
3. It needs consultation of internal and external experts.
4. It is a long and time-consuming process.
5. It involves in-depth planning with evidential testing.
6. It is a capital intensive strategy.
7. It helps to utilize all available resources optimally.
8. It leaves a permanent effect on the structure of the sick company.
9. It needs full co-operation of people associated with the sick company for its success.

Types of Turnaround Recovery Strategies

1. Cost efficiency strategies

Most companies implement turnaround recovery strategies in the pursuit of cost efficiencies. Cost efficiencies entail a varied range of actions aimed at producing quick wins for a company. The measures may improve a company's cash flow or stabilize its finances before coming up with more complex strategies.

Cost efficiency strategies are often implemented first in any recovery strategy. Companies prefer turnaround recovery strategies that achieve cost efficiencies because they are easy to implement, require little capital, and their effects are almost immediate. Cost-oriented turnaround strategies include reducing (R&D), stretching accounts payable, eliminating pay increases, reducing accounts receivable, cutting inventory, investment diversification, and reducing marketing activities.

The measures can be accompanied by reduced pressure from debt repayments through financial restructuring. However, such an action carries some risk. Companies that solely rely on cost-cutting as a turnaround recovery strategy risk face increased staff turnover because of the reduced employee morale. Cost efficiency strategies can also damage the resources necessary to maintain a company's core focus.

2. Asset retrenchment strategies

Companies that face performance decline usually pursue asset retrenchment actions after a cost-efficiency drive. Under the strategy, companies evaluate underperforming areas to eliminate them or make them more efficient.

The usefulness of retrenching assets as a turnaround recovery strategy depends on a company's ability to generate cash flow. For example, a company may dispose of its old assets to generate cash or invest in new ones.

3. Focus on a company's core activities

Companies also resort to focus on their core activities as a turnaround recovery strategy. Under the increased focus, companies identify markets, customers, and products that can potentially generate high profits, and adopt the measures as the main focus of the firm activities.

For example, a company may re-focus on loyal or less price-sensitive customer segments or product lines best known to it. It may develop a clear competitive strategy through focus.

4. Change of leadership

Companies often replace incumbent CEOs as a turnaround recovery strategy. During turnaround situations, most companies appoint new chief executives from outside the company as a way of injecting a new way of thinking into the top management.

It is inspired by the idea that CEOs bear the responsibility for a company's negative position, and their replacement serves as a signal of change. CEO replacement can always be accompanied by an overhaul of the top management team to avoid repetition. As a result, a new senior management team can enable a company to focus on new strategies to lead the turnaround.

Model Questions from UNIT -II

I. Short Notes

1. Industrial Sickness
2. What is Crisis Management?
3. Turnaround Strategies

II. Essays

1. Explain in detail about Causes and Consequences of Industrial Sickness.
2. Explain the Types of Crisis.
3. Briefly Explain the Types of Turnaround Strategies.