

# **CORPORATE MANAGEMENT IN THE CONDITIONS OF CRISIS**

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**Monograph**



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## INTRODUCTION

Every enterprise exists in a particular business environment, which can be considered as adequate if a real working market mechanisms are functional and on the basis of a supply and demand as well as on the economic policy of an economic centre, the production factors are efficiently appreciated. If such a status is disrupted, it can result in a variety of problems and a subsequent crisis.

Current hypercompetitive and global environment is recently significantly influenced by the global financial and economic crisis, which destabilises the business environment in Slovakia as well. Gradually the occurrence of enterprise crises increases and the range of possible crisis causes in the company grows. The environment variability and constant changes in the enterprise, increase the requirements for the management, which must be able respond to the adverse situation quickly and in a timely manner, and if the company is undergoing a crisis, the necessary tools to ensure its overcoming in the development of the enterprise have to be implemented. Business management in the crisis forces the corporate managers to use innovative methods and management techniques that are adequate in the environment that has the nature of the crisis.

Crisis management is a management tool, whose correct timing and effective use is a prerequisite of success and the possible reversal of a negative situation in the undertaking. The long-term application of the crisis management practice has a negative impact on the corporate culture. It is ideal when the period of the crisis management does not significantly exceed the horizon of one year. With the high extension of this period there is the problem with development direction of the enterprise as well as with the release of a creative potential. It is not uncommon that the fast and efficient overcoming of the crisis can help increase the integrity and loyalty of employees with the company.

Despite the fact that the corporate crisis is a natural and organic part of the life cycle of the enterprise, it is becoming a current and serious problem of all economies in the world. Not all enterprises can manage to overcome the crisis and to continue in their activities. For many enterprises the crisis represents a situation, when the further existence of the enterprise is threatened and the enterprise is going to decline or demise/terminate.

It is possible to deal with the decline of the company via restructuring, which is one of the methods to overcome the crisis and reverse the development crisis. The problem of restructuring the enterprise can be understood as a forced response, or as a result of the enterprise encountering the certain boundaries in its development.

The number of enterprises that take the advantage of the restructuring to reverse its adverse developments constantly grows. The restructuring process is generally understood as a specific methodological approach to the enterprise resource reallocation. As one of the possible ways in which the company management changes, it contains the rights, responsibilities and relationships of all subjects' corporate activities. In general, we can say that the optimization of these elements is the basis of any of internal and external restructuring efforts.

The number of enterprises which in case of bankruptcy occurrence, i.e. increasing or insolvency make use of the extension of the judicial institute, which, unlike the bankruptcy restructuring, allows the company to continue in their activities also gradually increases.

Termination of the enterprise, which may be due to the failure to deal with the corporate crisis, brings not only the loss for the enterprise owners, but is an economic loss to the national economy as well. The dismissal of employees of the unfunctional enterprise increases the unemployment and spent resources in the form of deposits quit to be appreciated. There are losses for the business partners, banks, shareholders and the cities lose the local taxes and fees, and development in the form of sponsorship.

*Authors*

## 1 CRISIS AS A NATURAL PHENOMENON OF ENTERPRISE EXISTENCE

The business enterprise is the fundamental entity in the market economy. It has its typical traits and characteristics of a target-oriented system, the objectives of which form the basis of the business strategy. The highest corporate goal is **to ensure the growth of the market value of the company and its existence**, what can be achieved only if the enterprise is economically strong, i.e. if it is properly funded.

**Every business goes through several stages of development since its inception.** The existence of the business as a business entity is limited in the beginning and the end of the business. The life cycle of enterprises can take decades, centuries, and eventually it does not have to end in its elimination, or, it can take only a couple of months, at most, a couple of years time can between its origin and elimination. There are few theoretical views of the existence and development of an enterprise. The best approach to the development of the enterprise is the enterprise life cycle curve.

### 1.1 Curve of the life-cycle of enterprise

The life cycle of the enterprise development company, its position on the stage speaks volumes about the market and constitutes a source of information for forecasting the future existence and development of the enterprise. The life cycle of a business model illustrates the period since the inception of the company until its demise. It reflects various aspects, such as economics, technology, production, and so on. The curve of the life cycle of an enterprise varies depending on the position of an undertaking on the market and the situation on the market. The curve is determined by the life cycle of products, which the company manufactures and sells, and determined by many internal and external factors affecting the activity and success of the enterprise.

The existence of a company usually is not straight forward and a theoretical model of the life cycle of a greater or lesser extent, only copies. A graphical view of the life cycle of an enterprise by means of income and expenditure, depending on the time is shown in Figure 1.1.

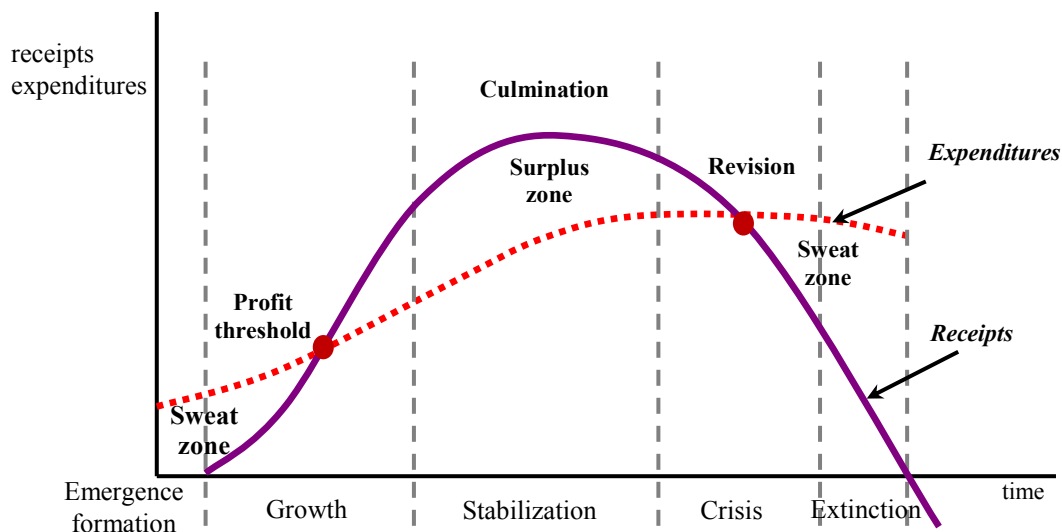


Fig. 1.1 The curve of the life-cycle of enterprise [105]

For the representation of the life cycle of an enterprise we use a chart where the axis of "x" is the time factor and "y" is the volume factor that can be represented by the amount of the capital expenditures, revenues, expenses, income, production and the like.

The curve of the life cycle of an enterprise is determined by the curve of the life cycle of products produced and sold by the company. The market success of the products and services of the enterprise is successfully copied, and the effectiveness of the undertaking.

The model of life cycle of the enterprise consists of several stages, in which an enterprise can, but does not have to go through during its existence. One of the fundamental stages of the life cycle of the enterprise includes:

1. establishment and the inception of the enterprise
2. business growth,
3. stabilization of undertaking,
4. the crisis in business
5. the demise of the company.

The total length of the life cycle of the enterprise and the length of the various phases of the life cycle of individual businesses vary. The period between the establishment and the demise may not always include all phases of the life cycle, it can, for example, come to a crisis, or a demise before the company reaches its stabilization. The course of the business cycle is affected by the internal and external business conditions, for example, the business activity of competitors, state fiscal policy, innovation policy, qualifications of enterprise workers, security, security of the transformation process and logistical activities, which affect the activity and success of the enterprise. The life cycle reflects the degree of the enterprise development, its position refers to the market and constitutes the source of information for forecasting the future existence and development of the enterprise.

### **1.1.1 The establishment and the demise of enterprise**

The process of establishment a business is a complex decision-making process that is completed by the establishment of the company. In the beginning of this process, there is the idea of the future entrepreneur or entrepreneurs verified by means of the analysis of the future market, the analysis of the personality of the founder and the analysis of the available financial resources, which requires the implementation of business ideas. Part of these analyses is to develop a business plan.

At this stage, it also decides on the organization-legal form of the enterprise. The issue of the necessary amount of the equity capital, obtaining the credit, subsidies, the distribution of business risk, profit sharing, etc. It should be dealt with as provided for in the Commercial Code. Enterprise starts its official existence by making an entry in the commercial register.

### **1.1.2 Business growth**

**The business growth** represents the assertion of the business on the market and the adaptation to the market. The growth curve begins by the phase in income, which should have a sharp development and be as soon as possible at the point of a profit threshold intersect the curve of expenditures. The profit threshold changing the sweat zone of the enterprise life-cycle to the surplus zone, in which the revenues exceed the expenditures of the business,



which achieves a positive cash-flow. The growth phase is completed at the time when the curve revenues and expenditures lose its steepness and are relatively stabilised. Then the company promotes successfully on the market, and creates thus the conditions for its growth.

Business growth can be achieved by:

- **Internal growth**, in which the enterprise more efficiently makes use of production factors embedded in its founding, such as land, buildings, machinery, equipment and supplies. Effective use of assets and personnel to increase the volume of production, the diversification of the products leads to the sales increase of products in the existing market. Businesses must constantly look for more options for the introduction of new, innovative products, for current and also new markets. Internal growth can also be achieved by own investment activities, by the profit, the development of innovation, structural changes and the growth of the quality of products and services in the competitive environment. The motivation of workers to achieve better results has an important place as well.
- **External growth**, in which the enterprise makes use of external sources of funding, additionally inserted assets, or by admitting another shareholder, or by business combinations in the form of mergers or Joint-ventures.

Dynamics of business growth is manifested by:

- A **quantitative growth in the form** of a turnover increase, growth of staff, increasing the assets, and so on.
- A **qualitative growth in the form** of increased company prosperity characterised by:
  - turnover growth,
  - stable, or increasing market share,
  - steady, or rising prices of products,
  - stabilized, or decreasing costs,
  - rising profit tendency.

In order to sustain the company's growth and smoothly get into the stage of stabilisation phase, it is necessary to develop other business activities, such as:

- rigorous market analysis and the choice of an appropriate pricing strategy,
- growth of the products quality and the introduction of new or innovative products on the market,
- implementation of a number of support activities.

The growth must be part of a comprehensive business development in taking the internal and external forces into account. The strategy for the growth should be contained in the company's strategies, in the opposite case, if the company growth only reflects the changes in the external environment, it comes to the growth of business risk.

The only way to ensure the future growth of the company, is to create the second growth curve before the first curve starts to fall. This requires constant inventiveness and creativity. Enterprises must learn how to search for and exploit the opportunities for the growth. The business growth requires invocation of the new wave of interest in products. It

means to have more valuable and attractive offer for customers than the competition, or another offer, which the customer strictly wants to possess.

The business growth strategy can take two basic forms:

- **Growth in existing markets.** Also the well run company has to be continuously maintained, developed as well as it has to search for new opportunities to enhance its performance. A global product requires knowing the needs of different geographic markets, different cultures and local preferences, so that it is competitive also locally. This means:
  - increase the sales success,
  - increase the effectiveness of existing trade through the growth of sales of the most profitable products, satisfying the needs of clients, and by the growth of the share of the expenses of the customer,
  - acquire new customers,
  - offer new products and services,
  - create new segments within the existing market.
- **Growth by the access to another or a new market.** It is important to recognize the potential in other markets, to choose a strong competitive strategy, to differentiate and get customers from the competitors already established on the market. The opportunities to grow are via:
  - entry to another segment of the existing market,
  - entry onto the market of customers,
  - entry onto the market of limited partner,
  - entry onto the market of suppliers.

Businesses do not have to constantly compete with the competition. New markets are known just by being an unspoilt area and create opportunities in the pursuit of high profits. While some of the new markets arise entirely outside the confines of the existing industries, most of them origin by the way that leads to an extension of the existing borders of the industry. The competitors are losing thier power on the new markets, because the the rules of the game are not laid down yet.

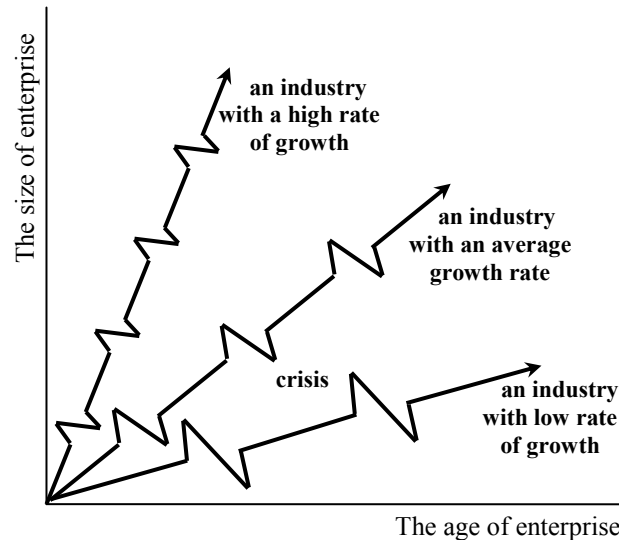
#### **1.1.2.1 Model of evolution and revolution in the development of the enterprise**

The model of evolution and revolution compiled by Larry Greiner is one of the life-cycle models. This is a simple model, where the rotation movement of the evolutionary and revolutionary phases are shown. The author comes out from the assumption that the future is determined mainly by its own historical development, and not by external factors.

According to the model of evolution and revolution (Figure 1.2) are the basic factors that influence the development of the enterprise at the time:

- the age of the enterprise,
- the size of the enterprise,

- the growth rate of the sector concerned,
- evolution,
- revolution.



**Fig. 1.2** The development of the enterprise at the time and, depending on its size [31]

From the Figure 1.2 it is clear that the higher growth rate of the industry, the faster the changes occur in the development of the sector and at the same time crises arise, which are illustrated as an interruption of the continuous development of the industry.

Development of business, according to Greiner, consists of five development levels. Each level is associated with the presence of Hegelian dialectic entities, evolution and revolution:

- **Evolution** is defined as an extended period of steady business growth in a given stage of development. The activity of the enterprise is almost invariable throughout the period of evolution.
- **Revolution** means that part of an enterprise which is associated with the essential development stages and turbulent changes in the existence of undertaking. It is associated with the company crisis.

The different levels of enterprise development are characterized by the management style that is predominantly on the level of development, and by the subsequent crisis, which is characteristic for the level given. The various levels of enterprise development and special crises for the given level are:

- **Creativity and crisis management:** the company is young, and its growth is supported by the creativity of the founder. In undertaking works a few employees, everyone is familiar with each other, share their experiences, knowledge and information, and the communication between them is frequent and informal. There is a crisis of leadership. Business needs strong leadership, to be determined by an appropriate organisational structure.

- **Crisis management and autonomy:** an undertaking which survives the first stage and is capable managers, usually enters the successful period of growth. At this stage of the highly centralized, the enterprise has a functional organizational structure, there is a specialized function, communication becomes more formal. There is a crisis. The solution is the delegation of powers. It is difficult for the owner to surrender their powers and responsibilities of the managers.
- **Delegation and crisis control:** the company is focused on the motivation of employees. This stage enables a business to expand. There is a crisis.
- **Coordination and crisis** for the company is characterised by the use of formal **bureaucracy:** systems to achieve greater coordination and taking the responsibility of senior management. Decentralized business units are merged into product groups. The aim is to ensure a more efficient allocation of limited resources the company growth. There is a crisis of bureaucracy.
- **Cooperation and psychological saturation crisis:** the company focuses on quick problem solving through team work. The most commonly used matrix organizational structure. There is a crisis in the field of the psychological satisfaction of employees, which depletes the intensive teamwork and constant pressure of the need for innovation and new solutions. This crisis can be addressed by the new programmes and structures that allow employees to relax and recharge with new forces on a regular basis [31].

The model draws attention to the fact that the solution to every crisis in the enterprise requires a move to higher levels of the life cycle of the enterprise. Greiner on the crisis in particular, cooperation is recommended.

#### **1.1.2.2 Models of growth enterprise crisis management**

The life cycle of the enterprise development company, its position on the stage speaks volumes about the market and constitutes a source of information for forecasting the future existence and development of the enterprise. On the course of the business cycle affect the internal and external conditions for business, for example. the business activity of competitors, state fiscal policy, innovation policy, enterprise security, logistical activities, security personnel qualification the transformation process etc.

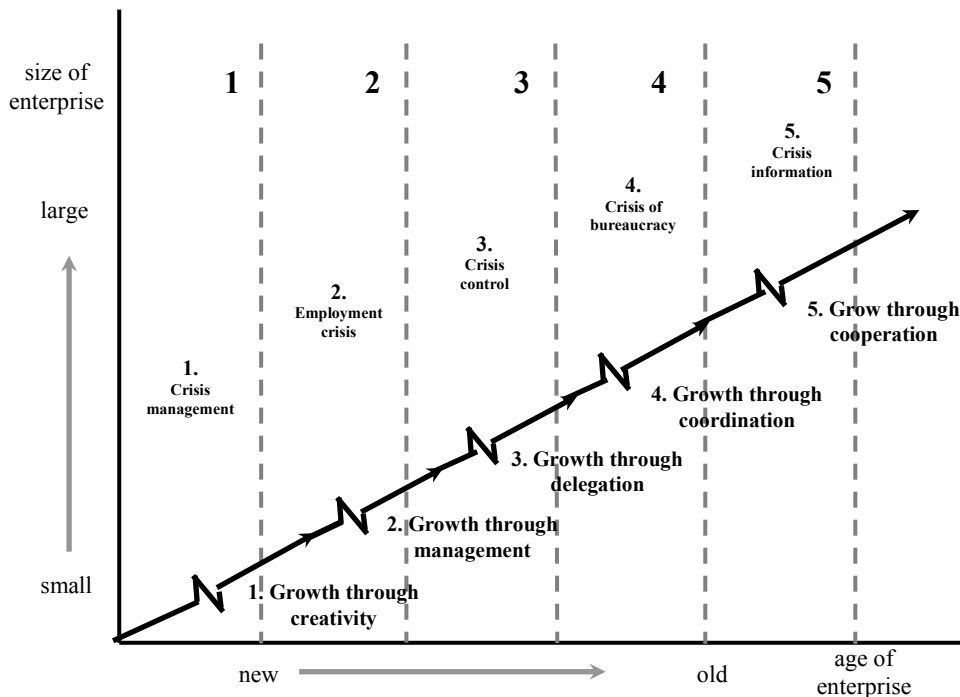
Phase of the crisis is partly situated in the zone of the surplus, in part after the point of the revisions in the sweat zone. The onset of the crisis in the zone of the surplus is hard to reveal. It is only through a decrease in income, and the curve is identified by a decline in profits. This condition can result from lack of market position, from a higher cost compared to its competitors, or other weaknesses of the business activities

Given the progress of the life cycle of an enterprise is to some extent idealized. Due to several reasons, an enterprise may get to the stage of the crisis and the subsequent demise of the at any time during its existence. Often there is a crisis and the demise of the stabilisation phase, possibly without, after a phase of crisis does not occur, but further growth.

To make the transition from the stage to the stage of stabilisation of the crisis prevented the undertaking, it is necessary to constantly compare his position with the competition. This is mainly an analysis of market share and economic results by means of benchmarking.

#### 1.1.2.2.1 Model crises business growth by Howard Grosier

Already at the stage of business growth can sometimes occur several types of crises. These crises can cause premature termination of an undertaking. In the diagram of the Howard Grosier in Figure 1.3 shows the dependence of the size of enterprise and his age. At the same time are the most commonly identified cause of the crises, which can disrupt the continuity of the business growth and potential ways to overcome these crises are outlined [107].



**Fig. 1.3** Stage of business growth – Howard Grosier diagram [107]

In the initial stage of business growth is a small newly established enterprise, which must resolve the initial crisis management situations. The key to overcoming them is the creativity of the owners of the business or individual companions.

In the next phase of the company of medium size, which requires a division of labour in the management. Growing demands for a separate implementation of each activity, for this reason, a number of specialized managerial and executive activities arise.

The company will continue to develop and gradually have a managers decision makers. However, the possibility of abuse arises in the case of a conflict of interest. This phenomenon can be prevented a permanent control. The process of checking is necessary to delegate so that it is permanently controlled by the entire management and executive apparatus.

If the undertaking is sufficiently large and mature, there is a potential risk of developing crisis of bureaucracy. To overcome this crisis can be consistent the decentralisation of decision-making powers, which is expected to result in a completely autonomous status of the former in-house units, headquarters management coordinates the business activity only.

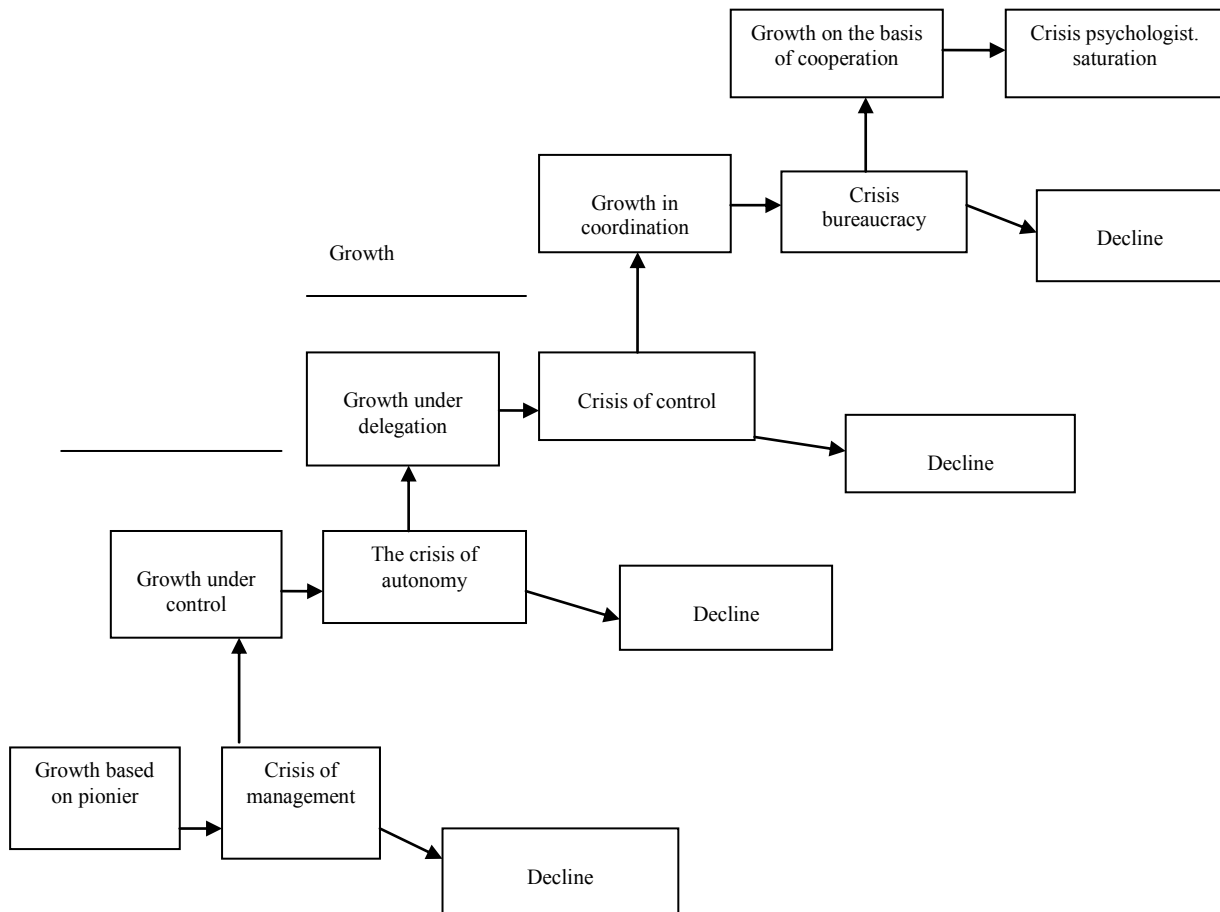
The last phase is typical for large enterprises and conglomerates, where management has the responsibility of only the headquarters strategic direction. Here is an important cooperation of associated enterprises.

From the Figure 1.3, to see that the crisis may occur in any of the 3 stages of development of the enterprise. It just depends on what you choose the way to her leadership, quickly identify and eliminate. If the company finds a negative change in the market area, or the drop in revenues, it begins to apply the crisis management. It's a special kind of management, starting from the moment when the enterprise is forced to choose a distribution strategy.

#### 1.1.2.2.2 Model crisis business growth by Larry Greiner

The most important conclusion of the model according to Greiner is that the solution to the growth crises every crisis requires a move to higher levels of the life cycle of the enterprise. Greiner implies that the crisis caused by bureaucracy can be removed pionierskym management, delegation, or greater coordination, but rather through cooperation.

Another essential conclusion is that, if properly managed, is the most likely consequence of changes are not upadanie. In order to avoid him, the leadership must ensure that the transition to a higher level of growth before the crisis will cause too great a loss of energy and resources.



**Fig. 1.4** Life cycle of enterprise by Greiner [31]

The growth of enterprise crisis management model (see Figure 1.4) compiled by Larry Greiner describes five levels that the life cycle of the enterprise, including crisis and possible ways of dealing with situations arising. Each level of the model of growth crises are as follows:

### ***1. Pioneer and the crisis of leadership***

Most business plans are born on the basis of simple supporting ideas. One or more individuals with sufficient faith in the success that set up their own business, decides that they will try to implement your unique idea. Therefore, this evolutionary phase called creative. Many innovators in the field of electronics and software leaves the big corporations to be able to freely implement their ideas and thoughts. The world is full of almost unbelievable stories about successful entrepreneurs. who started in the garage of his parents, but has had an excellent idea. These are usually technical or business-minded enthusiasts or self-study and despise the classical organisational and management practices. Most of the natural entrepreneurial talent and not the managers. Their energy is focused on the production and sale of new products. Communication between employees is frequent and informal. Workers are working hard and long for the relatively low salaries. They expect that after you have successfully established a business in the market, will increase not only profit but also their wage. The success of an enterprise is determined by the feedback, in order to meet the requirements of customers.

At the moment of achieving success and increasing the volume of production is the need to address the issue of effectiveness. A growing number of employees, it is not possible to continue to drive informal personal contact. New employees no longer have to share the enthusiasm and dedication as former employees. The administrative requirements for an enterprise to grow gradually, decide who will take over the administrative leadership required and who will be responsible for the smooth running of the undertaking fully. There is a manager in the professional position which is acceptable to the owners, as well as for the employees of the enterprise. To overcome the crisis, "zero", is a necessary move to phase, which is characterized by a strong management.

### ***2. Management and crisis of autonomy***

After the takeover of the responsibility for managing the business of one of the partners or by the manager, to create the individual features, and the staff is specialized in the relevant places. The management of the company is gradually evolving into a business unit with too diverse organisational structure, with fixed rules and the system. Communication becomes more formal and less personal, and adheres to the hierarchical arrangement of the enterprise. The management structure in the management level begins. Executive committee decides on global issues and lower levels of government, provide the individual activities of the undertaking covered by the specialized functional managers. Management methods of direct control and improve control in the enterprise increases performance.

The next crisis occurs when employees or owners are finding that the existing organizational structure of their actually restricts and prevents them from making decisions. Mechanical structure, which has proven itself in dealing with previous crises, is unsatisfactory and is involved in the crisis. Employees at the lower levels in the company feel that the leadership does not attempt to solve their problems, knows no such problem and does not understand them. Managers at lower levels for more power and freedom when deciding on common problems.

Managers at lower levels of governance are mostly familiar with the local market better than their superiors. Yet they are overwhelmed by the fulfilment of orders that threaten their initiative and do not give them space on their implementation. Higher levels of management is getting into situations that deal with deciding on unnecessary, often even outdated cases and issues that are not relevant for the enterprise. The situation is not in a business typically none

sufficient prepared. On the one hand, the top executives don't want to lose the ability to make decisions and take responsibility, on the other hand, managers at lower levels of governance do not have sufficient experience to be able to decide for themselves.

### ***3. The delegation and crisis control***

In order to resolve the crisis, which is caused by zero – the ability to control, it is necessary to delegate some powers to the lower levels of management. Business growth can continue, but it must be ensured that the decentralisation of what motivates subordinates of managers in the business. Gain greater powers, but also responsibility, which has so far only had higher levels of management. As an additional incentive factors are profit centers, and various types of bonuses. Executive Committee focuses on the control of deviations, which is based on the regular reports. Communication between management and subordinates is less regular services, limited personal contact and information – means of communication are used. The task of leadership is to look for new business activities, which operate in addition to the already established activities.

Organic directory, which contains the necessary access delegation, is a source of loss of control in the company. Autonomy business services leads to suboptimal solutions from the perspective of the enterprise as a whole and the conflicts between the departments. Lower the head, for which they were conferred considerable powers begin to exceed its powers and cease to be interested in the overall coordination of the plan, financial and human resources with other organizational units. Management losing control of making profit and is not capable enough to affect the specific objectives and activities of each of the subordinate sections. Crisis arises when the executives trying to take control of businesses returning to centralization, which is a large and rozvetvenom business very difficult.

### ***4. Coordination and crisis of bureaucracy***

Loss of control should be confronted with a variety of mechanisms for coordination. Formalized planning procedures, adequate staff personnel, cost models and incentive system must be implemented companywide so as to promote the objectives of unity in fragmented decentralised structure of the enterprise. Some features, such as data processing or the personnel system should be part of the centralized, with regard to the management of the undertaking and other functional parts of the breakdown between more carefully. Decentralized units are linked to groups that should be chapane as investment units, which are carefully analyzed by return on investment. Local managers need to recognize his subordination to senior management and the enterprises should be connected through a more sophisticated mechanism of coordination. At the same time, it is necessary to increase the identity of employees with the company using the system benefits. All of the above methods of coordination is useful, in terms of the efficiency of resource allocation..

Loss of control should be confronted with a variety of mechanisms for coordination. The company continued to grow, in this mode, can lead to depression, which causes the wake of bureaucracy. The differences in the local and global rules and regulations, unnecessarily complicated paperwork and information links is stifling innovative approaches to solving problems. The current size of the business makes it difficult to effectively manage ongoing through formalized coordination. There are conflicts between the scheduled and staff workers. Lineage the head of the governing councils of the specialists, who do not know the particular situation of the undertaking and then complain about the reluctance of scheduled senior leader staff. Management and coordination of the method are compared to the benefits that they



bring, expensive. Corrective receive priority over the disgrace of the solution to the problems. Innovation is almost unfeasible. The enterprise is too big and it is not possible to control rigid programs.

### ***5. Cooperation and psychological saturation crisis***

Fifth, the last level of growth is cooperation. In order to overcome the crisis is to apply the concept of teamwork and the management of interpersonal relations. Dual authority resulting from the temporary project groups and created the original functional bodies, leads to a condition called shared responsibility. Social control and personal discipline among employees is replaced by a formal control. The new system is characterized by greater flexibility and access management behavioral. Is to create a team composed of workers of different professions, who have different hierarchical position, gradually reduces the number of staff workers in the management of their business integration to individual teams, which advise and help. Enterprises are engaged in various forms of matrix organizational structures. The previous, rather formal system is transformed into a multi-purpose system easier. Consultation officers are focused on solving problems. Training managers emphasizes on human resources management, team collaboration and conflict resolution. The information system is designed to provide up-to-date information for the decision-making process. The physical involvement is focused more on the result than on the results of the team members. Creating a suitable climate for experimentation with new methods. A formal check payable self-discipline commands and recommendations. Such organisational structures exist in large technology based enterprises.

Currently, the most well established large companies located in the fifth stage and preparing for a possible crisis. Greiner itself predicts that enterprise based on collaboration will result in a crisis, that will be a psychological saturation insulin resistance. Managers and employees are finding that they have a duality of leadership and stress from challenging teamwork go energy. The dual needs of mechanical control and flexibility to your employees, broadcast services, various, often conflicting signals, who then suffer mentally and physically.

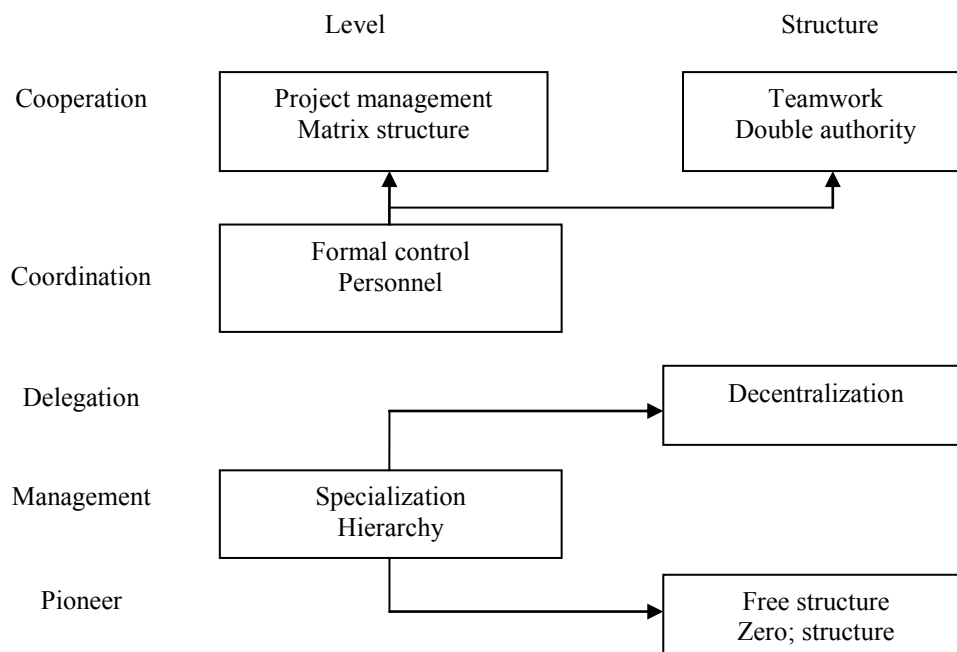
One of the possible ways of resolving this crisis is a proposal for the sixth stage and the emergence of so-called dual organizational structures. The employee would normally carry out his work in the organizational structure. Then, what would be the physical and psychological grew tired, passed into the "reflecting" structure, in which he worked on his next career as through training and other creative forces gathered would. The stage would be repeated at regular intervals, such as a quarter or half-yearly cycles. After a certain time, for example after a period of five to seven years, would receive about half a year fully paid off, which would be used at the discretion of the continuing professional growth. Taking care of employees is one of the most important conditions for the success of the enterprise and managing corporate crises. Workers are provided by the rest files, but also from the stimulus of educational services.

Other authors who have this concept, however, the further development of this emotional crisis and its possible consequences, are not comfortable with laconic or more, none the less concise statement and the next crisis is sure to come.

### 1.1.2.3 The impact of growth on the organizational structure of a business undertaking

A brief explanation of the Greiner growth of the model indirectly points to the constant movement between the organic and the mechanical type of organizational structure of the enterprise. The next Figure 1.5 below shows how each of the life-cycle of enterprise level gives momentum to the shift in the way the leadership to more:

- **mechanical type** – stop put on the requirements and specific work on the part of senior management,
- **organic type** – rules are minimal and are awarded rather than individual leadership is decentralized, as workers collect information and identify yourself to the task.



**Fig. 1.5** The transition between the mechanical and the organic organizational structure during the existence of the undertaking [31]

Enterprises in the process of pioneer (creativity) are more organic. Control plays a minor role, the differentiation is minimal and the power is concentrated. On the management level is dominated by mechanical features, which are tasked to bring an enterprise from crisis management. The delegation is to release through decentralisation. When the freedom, there is a strengthening of coordination. In growth on the basis of cooperation, make use of both forms of structures, that in this way, create a complex type. In other words, a dynamic view of organic and mechanical parts brings Greiner holding companies.

The conclusion is that comparative table 1.1, which is based on the phases of the life cycle of the enterprise by Larry Greiner.

**Tab. 1.1** Phase of the life cycle of an enterprise and the characteristics of the company [31]

Phase	Basic tasks	Organizational structure	Leadership style	Control system	Encouraging workers
<i>Pioneer</i>	Sale Production	Informal Liner	Business Individualistic	Market success	Ownership
<i>Management</i>	Production efficiency	Centralized Functional	Direct management	Standardization Cost centers	Wage Growth of wage components
<i>Delegation</i>	Expanding the market	Decentralised by region	Delegation of powers	Reports Profit centers	Individual awards
<i>Coordination</i>	Consolidation	Liner -staff and component manufacturing	Documenting	Planning and investment centers	Share of profit
<i>Cooperation</i>	Innovation Redevelopment	Teamwork	Participation in the management	Common goal	Rewarding team

This model puts a stop to the role of a Manager in the management of the enterprise. The foundation is a good time to recognize the crisis and be ready enough so the incoming to only a minimum part of the odčerpala energy and resources of the enterprise. In terms of the organizational structure of this model is only temporary, and when they wear out, it must be changed. Each structure is morally or physically wear out after a certain time. It is difficult to capture the moment of moral obsolescence, which is suitable for a change. Managers often have a tendency to deal with all the problems, but in another, as selected and applied the structure of an enterprise.

Confirmed detection of organic and mechanical structures, rotation and expansion of production, control and subdued self regulation, monetary and non-monetary incentives for workers and owners.

### 1.1.3 Business stabilization

The whole phase of stabilisation is located in the zone where the revenue surplus in excess of the expenses. The overarching point of the curve is the point of culmination, in which an enterprise income tax reaches a maximum income. Beyond this point, although part of the revenue drop, it is however a slight decrease, which is not dangerous for the enterprise.

To venture into the phase of a crisis it is necessary to perpetually analyze the move prevented the position of an undertaking compared to the competition. This is mainly an analysis of market share, economic results, and so on.

Most businesses will reach the stage of stabilisation after a phase of growth. Some firms remain stable longer, others grow old quickly. There are also cases in which businesses will experience a revival, as the next phase of the life cycle, for example the acquisition of new markets, thereby achieving a growth of market share. It is one of the most important factors, market share which affects the position of the enterprise in a competitive environment, which can be defined as follows:

- **Dominant position** occurs normally with monopolies, or in heavily protected technology leadership position. This is achieved when at least 40 % share on the relevant market.

- **Strong position** is typical for an economically strong companies that can create independent strategies of competitors. This is achieved in less than 40 % of the market share on the relevant market.
- **Position a suitable** undertaking on the relevant market, if there is no emergency in the economically strong competitor.
- **A permanent position** on the relevant market is a private company, which has some specific advantages over other competitors, for example, achieves an extraordinary quality.
- **Weak position** economically strong competition, which is triggered by weak competitors in a given market cannot face.

The weak position of the enterprise on the market usually raises the completion phase of stabilization and transition to the phase of the crisis.

#### **1.1.4 Business crisis**

Phase of the crisis is partially situated in the surplus zone, and partially after the point of the revisions in the sweat zone. The onset of the crisis in the zone of the surplus is hard to reveal. It depends just on which way is chosen by the management to identify and eliminate it quickly. If the company finds a negative change in the market area, or the drop in revenues, it begins to apply the crisis management. It is a special kind of management, starting from the moment when the enterprise is forced to choose the distribution strategy.

It is challenging to recognize when it is just about the periodic fluctuations in the performance of the company and when the company actually gets into a crisis. A healthy venture is such a company, for which there are no doubts about his future. It is able to finance its activities, and to generate sufficient profit to meet its obligations, which is used to invest in the company and, ultimately, ensures adequate capitalisation of the shareholders' investments.

If the symptoms of an impending crisis in the enterprise are diagnosed or even the state of crisis, the crisis management determines the measures in the form of:

- **Enterprise Rescue Search:** the role of the corporate crisis is to facilitate business and solution methods of rescue to ensure the continuing existence of the company in the future. The essence of the life-saving techniques is to get in the business under the control of and manage their cash flows in order to minimize the negative and maximize the positive cash flows coming to the company. We can include the following remedial treatments to these methods:
  - **Method to rescue the enterprise without its legal and property demise**, which include consolidation, restoration, out-of-court settlement, restructuring and reengineering.
  - Methods to rescue the enterprise, which result in its legal and formal demise, including business combinations.
- **Liquidation of the enterprise**, which means the cessation of activities of the enterprise and the subsequent dissolution of the company. **Destructive methods** of dealing with the business crisis lead to the company demise and to the settlement of its legal and financial relationships.

### **1.1.5 Demise of the enterprise**

An enterprise may be terminated in two ways:

- **Legal and formal termination**, which is possible in the form of:
  - acquisition of companies,
  - merger of companies,
  - division of companies.
- **Material demise**, in which the company is terminated, due to the following reasons in particular:
  - expiry of the period for which it was founded,
  - fulfilment of the objective for which it was established,
  - voluntary decision of the entrepreneur,
  - death of entrepreneur,
  - judicial decision,
  - preventive liquidation,
  - forced decision based on the Act on Bankruptcy and Restructuring.

The complete demise of the enterprise is not only formal but also material, when the company ends its business completely and leads to **liquidation of the enterprise**. At the time of the company liquidation, it is assumed that income from the sales and receivables are sufficient to meet all obligations.

## **1.2 Model of life cycle by Miller and Friesen and its utilization**

Danny Miller and Peter Friesen [31] compiled the life cycle of an enterprise on the basis of their long-term observation of the development of 36 American companies from different sectors. The model consists of five stages of the enterprise life cycle:

### **1. Birth**

The enterprise is **simple and centralized**. The powers and responsibilities are concentrated in hands of the **manager-owner**, who does not use the delegation. Rank and file employees and officers are used in the management at minimum. Highly qualified technicians and specialists are used rarely. The enterprise is homogeneous and operates mostly at the close of the market. The businessman has in his hands most of the powers and the administrative responsibilities are at minimum. Companies are creative at this stage, they flexibly respond to changes in the neighborhood and are constantly look for niches in the market. They have a simple information system and a decision-making model.

### **2. Growth**

In the growth stage the businesses deal with more administrative problems, because they are larger, more diffuse and serve more markets with a variety of products. Their

structure is generally more complex, but less centralized than in the beginning. It is a functional organizational structure, the main departments are marketing, production, finance and development. In the ordinary routine the owner is of a minor role. More effort is devoted to the collection of information, control and coordination of the various operations. The number of technical-economic workers, accountants and managers grows. The executives are increasingly involved in the management and decision making, there is a lot of innovation, although less than in the first stage. The transmission of information and ideas is simple and fast. In deciding modern information systems start to apply broadly, the part of authority is delegated to the medium level of the control, the processes start to be formalized and more sophisticated corporate policy origins.

With the growth of the company its organizational structure changes as well. The transition from the birth through the growth to the maturity can be simple or more complex. It depends on the experience and knowledge of managers and management about the needs of the development of the organisational structure. The company must be able to successfully survive in a constantly changing environment. Changes and movements, which can be at least anticipated and be prepared to them, can be managed quite successfully.

### **3. Maturity**

In the stage of maturity the enterprises start to be more conservative and surrounded by more stable neighborhood. Their structure is mostly similar to the one that was applied at the stage of the growth. The company is controlled by the formal structure of lineage-bureaucratic type, procedure of making decisions is a formalized staff than in the previous stage due to the stable area. The tendencies to project more centralization project appear, less powers are delegated than in the growth stage. The efficiency is achieved **by using the activities and management processes automation**, however, which can in turn lead to the increases of administrative costs. Larger events require a quality information system focused on the analysis of the enterprise costs.

Mature businesses must be in productions. The role of management accounting grows, and so there is the division of the financial section, for example, management accounting, financial accounting, wages and salaries department and financial settlement roadmap and the analysis. The need for innovation plays a key role, the company is still ready for changes, which in turn draws energy and leads to the reduction in performance and decline in the enterprise competitiveness.

### **4. Decline**

The main cause of the beginning of the enterprise decline is the **change in the immediate surroundings**, from which the company draws the production factors and places its products and services. The growth of prices for the material, skilled labour or natural resources increases the costs of production and slows down the enterprise development.

The reduction of return due to the diminishing returns causes, that the costs are covered to a lesser extent. It has an impact on the declining profitability, which results in worsening of the access as well as in obtaining additional resources in the form of credits and loans to the banking market, which could help the company to overcome the temporary liquidity problems. Longer-term investments are not considered at the time. The company must realize the situation and respond fast enough and flexibly to it. The formal bureaucratic structure,

mainly applies to **functional breakdowns**, then to medium-developed centralization, information systems and decision-making methods.

Management in the phase of decline is accompanied by the existing three basic phenomena occurring in the declining companies:

- **Effect of pressure:** from the view of an individual, the general pressure is the most visible effect of the decline. With the company's shrinking resources and space for the incorrect decision decreases as well. For managers, it is harder to allocate the rare resources, because a poor choice can be the last point to the business decline. On the other hand, one good decision mainly does not cause a positive twist in the overall development. If the crisis lasts for a long time, it develops a dynamic and constant pressure on the labour to be done. Labour under pressure leads to less quality and incorrect decisions.
- **Effect of the conflict:** the allocation of scarce resources is one of the primary sources of conflict in the business. In the process of undertaking this issue is more exacerbated, since the smaller amount of resources, capital, labour and information has to be distributed to a larger number of needs. The different parts of an enterprise cease to be willing to help each other, because of their uncertain future, and nobody wants to be the one who will be restructuralised or even cancelled. Partial interests and competition make the cooperative management with involved in individual departments impossible.
- **Effect of the employees' leave:** the third effect of the decline is the movement of the labour force. Surveys show that particularly two types of employees are susceptible to leave:
  - *Workers, which would cover in the first place any involuntary unemployment:* less skilled workers, younger workers, workers on probation. The agreements with trade unions usually comprise the related order of forced leave due to higher adaptations.
  - *Workers leaving the sinking ship as soon as possible,* on the contrary, they are the most skilled workers, who have to find other employment. The leave of experts from the key positions even worsens the existing difficult situation.

Pressure, conflicts and problems require new approaches from the business management staff. The management of a declining business differs from the management of the company in the growth phase. Slimming down the company or return to a simpler organizational structure, does not solve the subject matter.

According to Miller and Friesen the companies in this stage are highly centralized. Even simple decisions are given importance at this stage and dealt with executives. Declining companies usually miss the correct information and control system designed for businesses. Vertical and horizontal communication is inappropriate, and does not reflect the ideas and suggestions coming from the lower level of the management. The decisions taken are conservative, innovation is rare and there is an effort to minimize the risk.

The conservative approach to the management means that of the maintenance of centralism is necessary due to the danger the existing situation brings. Maintaining the quality of employees in the company is a direct necessity for business.

## **5. Revival**

The most common question the managers ask at this stage is how to revive the company, what is necessary for the reconstruction and revitalization of the company's turnover. It means to deploy:

- aggressive development strategy,
- strong leadership,
- extensive austerity,
- rapid intervention into business,
- undertaking efforts to stabilize the area.

The revival is usually possible only if managers can take hard and often unpopular measures in respect of activities, resources, and people who are in demand even after the reorganization.

Miller with Friesen indicate that the highest diversification of production and the market, in which the business operates, occurs in the revival phase. Property is the same as in the stage of maturity, but scattered, the enterprise is bigger. In the enterprises some innovations appear and they are surrounded by or even the enemy surroundings.

The organizational structure is divisional, due to the new requirements of heterogeneous market and strategy of diversification. The centralistic system of management is no longer sufficient, and the executives are not able to solve complex tasks of the diverse market. Although the directors are fully responsible for their sections, the general policy is still determined by the management and control is ensured through a highly sophisticated information system. It is important to improve the planning system and the decision-making process. The power of operational decisions is delegated to the divisional level.

Companies are not afraid to take bold risks at this stage, an innovative analytical and thoughtful approach in decision-making is affected by the system on the basis of participation. Project groups are created to solve complex interdisciplinary and inter-departmental problems. In many cases, this is the most interesting phase, which produces the most sophisticated organizational structure.

Currently, companies begin to use increasingly the strategy of twist. *Twist in the evolution of an enterprise* means, above all, boost performance, efficiency and entrepreneurship. For successful application of the strategy of twist and reversion of the negative development in the enterprise, strong leadership is necessary. The strategy of twist may be based on:

- **Concept of the tipping point**, which draws attention to cost reduction and disposal of unproductive assets of the enterprise.
- **Concept of business reversion**, which draws attention to its production and marketing efforts to increase the enterprise income.

Both concepts are used to improve the position. First, the companies apply the performance twist that in a short time reduces costs for business and contributes to the



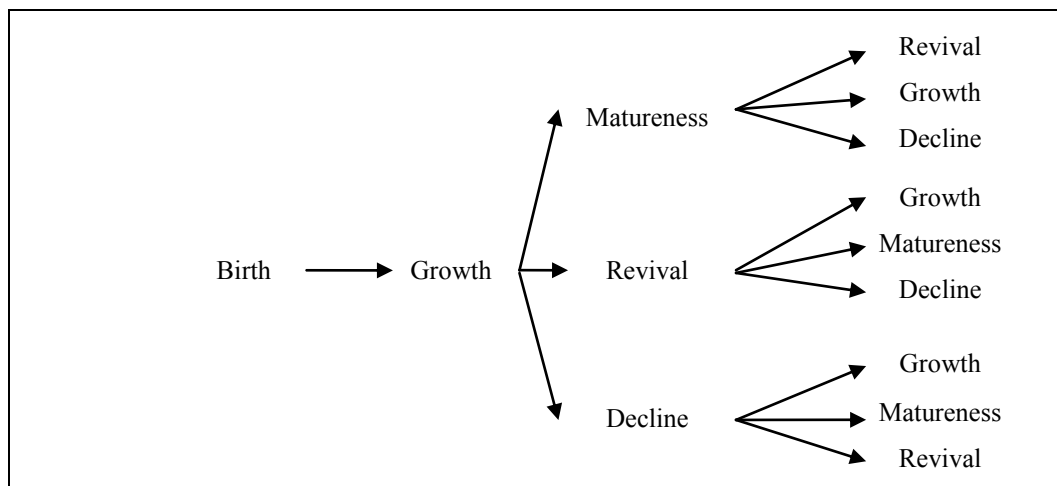
survival of the company and at the same time leads to the recovery of the cash flows of the enterprise. This strategy would save the enterprise from the worst and bring short-term success in the form of a zero income, or a slight profit. In longer term, this strategy fails. For the long-term improvement of the enterprise status and prosperity, it is necessary to apply the concept of a business reversion, which, if successfully applied, brings the company to maintain and grow profits.

**Tab. 1.2** Business performance and reversion in the enterprise development of [31]

Business twist	Performance twist
Change the product/market: <ul style="list-style-type: none"> <li>• new products and services,</li> <li>• increased emphasis on research and development,</li> <li>• quality production.</li> </ul>	Operating costs: <ul style="list-style-type: none"> <li>• increase worker productivity,</li> <li>• reduction in direct costs.</li> </ul>
Market share: <ul style="list-style-type: none"> <li>• price reduction,</li> <li>• vigorous application of marketing tools.</li> </ul>	Reduction means: <ul style="list-style-type: none"> <li>• increasing the use of machinery and equipment,</li> <li>• recovery/disposal of non-productive enterprise,</li> <li>• sale of unneeded assets.</li> </ul>

Life-cycle model also includes changes in the organizational structure of the enterprise. The layout of the enterprises in the course of life is changing from an informal to a more bureaucratic organizational structure.

Miller together with Friesen claim that none of the most common ways of life ends at the stage of decay. Figure 1.6 according to Friesen and Miller study shows the possible ways of the enterprise life-cycle development.



**Fig. 1.6** The enterprise life-cycle by Miller and Friesen [31]

Miller and Friesen point out the interesting studies on the relationships of various life-cycle stages of an enterprise, which may not follow each other in a classic (logical) order as mentioned above. Nevertheless, the birth is always the first stage. After the stage of growth it is mostly the maturity that follows, but some companies are transferred directly into the period of a decline or revival. For most enterprises, after the stage of maturity the revival follows, but some may start to fail, or even to grow again. The important thing is that even though the company is in the period of a decline, it can reverse this development and get into another stage.

## 2 CRISIS IN ENTERPRISE

The crisis can be seen as anything that has the potential to significantly affect and compromise the integrity and viability of the enterprise. Corporate crises may not be a reflection of the poor management of the company, but a reflection of the call for significant changes in the business.

Practice shows that businesses get into crises approximately every four to five years. Therefore, **the crisis is a natural and necessary part of the existence of any enterprise**. In principle, on the basis of the experience in the restructuring of enterprises, it is possible, depending on their performance and the efficiency, divide them into four basic types:

- **Apparently successful enterprises** that have good results, work and live with the idea that they do not need anything to improve or change. Many businesses that face such a life crisis, are surprised and not ready. Even in the best companies, there are things that you can do better.
- **Enterprises having problems with performance and efficiency** in comparison with the competition. The company is aware that something is not right, but often has no precise indicators to measure the performance parameters, or the lack of thorough analysis of the causes of lagging behind the competition. If the company is located in the described situation, it is necessary to prepare a thoughtful solution to each of the methods applied in the right places and in the right order.
- **Enterprises ignoring crisis performance**, and tending to its own degeneration. In the company there are a lot of unnecessary processes conserved as well as activities that are provided by the staff of workers. The stocks increase, fixed costs rise, communication and willingness to solve problems is limited. Employees considered this state normal. In this case, it is necessary to prepare a quick project of leaning the company, which should be very well thought out and drawn on the basis of a thorough analysis of all enterprise parts, in order to prevent the enterprise inoperability.
- **Enterprises with endangered existence** which are beginning to have problems with liquidity and begin to demise gradually. Troubles with the owners, trade unions, creditors, customers occur and there is in the danger of bankruptcy.

The various types of enterprises represent the position of the undertaking in the life-cycle of a crisis. Every enterprise will sooner or later gets into a crisis situation. The question is whether it will be tiny or large crisis. The enterprise's survival depends on the degree of preparedness, crisis management, the effectiveness of the implementation of the plan for the crisis team, quality and monitoring of the undertaking.

### 2.1 Definition of enterprise crisis

In 1991, Lagadec [67] defined the crisis as a *result of chance, unexpected events and destabilization*. The crisis should *be of exceptional, acute, urgent and dramatic nature* for the enterprise, whose task was to overcome the adverse and critical events for the enterprise. Crisis management has an important place in enterprises. A number of streams of crisis management, all of which have sought to provide solutions to the same problems:

- to understand why it is difficult to predict the crisis,
- start real efforts to prevent,

- to regain control over the activity of the enterprise..

Practicing the crisis management has been focused on the implementation of the priority risk-analyses, the creation of plans how to proceed in emergency, prepare and train managers to carry out simulation exercises, undergo masmedial training and practice communication techniques.

Frequency, types and forms of crises affecting the businesses is currently steadily growing. The terrorist attacks of 11 September 2001, represent more as a symbol than the beginning of a new type of events. The dramatic events create doubts of the ability to predict and cope with these crises, such as:

- climate disasters (warm wave in Europe, year 2003, storm in December 1999 in France, annual flooding, etc.),
- health crises (blood contamination, dioxins, asbestos, BSE, etc.),
- collapse of European and American empires (Enron, Parmalat, etc.),
- major industrial accidents (AZF, the Erika, Prežtíř, ...), and so on.

These events affect businesses, organisations, companies, political and economic circles and often leave the feeling that everything has gone wrong, in spite of the enterprises and the organizations declared readiness to cope with the crisis phenomena. Limitations of the current crisis management during the modern exceptional events appear.

***The nature of crises has changed.*** The crisis of today are different from those of the past. So far the practices used by the organisations to deal with the crisis are intended for the crisis of the previous generation. In many cases, traditional techniques are inadequate and unable to cope with the crisis situation. New forms of crisis managers often surprise, cause chaos, uncertainty and helplessness.

In the past, the crises developed commonly slowly and most of them could be avoided by professionally led planning, or at least blunt their effects. In recent years, the nature of many of the crisis situations changed dramatically:

- arise suddenly after a single event,
- very often they threaten not only the immediately affected enterprise, but the whole field, whole country, which is a consequence of the globalisation of markets,
- public is informed by media and pressure groups often negatively affect the deepening of the crisis,
- regarding the intensive automation, more and more businesses are much more susceptible to the crisis, particularly in the sectors depending on information and communication technology,
- businesses respond to the crisis situation inappropriately, clumsily, make quick hits, regardless of their subsequent effects.

Institute of Crisis Management defines the business crisis as: „*a significant corporate brakepoint, which stimulates the extensive media attention.*” The resulting monitoring of the

company affects its normal activity, and may also cause political, legal, financial and governmental influences on the business.

**Tab. 2.1** Overview of the definition of crisis [67]

Author	Definition	Scene	Characteristics of the process approach			Characteristics event access			
			action	combination	transformation	particularities	surprise	startup event	origin
<b>Herman (1963)</b>	– an event that surprised individuals to limit the time taken to respond and threaten their highest goals based	<i>aftermath dynamics</i>							
<b>Billings, Milburn, Schaalman (1980)</b>	– a situation that is the basis of the likely potential losses in a limited time to deal with it	<i>force dynamics aftermath</i>							
<b>Phelps (1986)</b>	– has become a necessity that requires immediate attention, and which may weaken the competitive position of the company	<i>force aftermath</i>							
<b>Nystrom, Starbuck (1984)</b>	– danger continuous existence;	<i>aftermath</i>							
<b>Müller (1985)</b>	– an unexpected event that threatens the existence of the company	<i>aftermath force</i>							
<b>Shrivastava, Mitroff (1987)</b>	– a serious threat to vital interests and most important objectives of the firm's survival	<i>aftermath</i>							
<b>Kovoor-Misra (1995)</b>	– events that are a threat to the survival of the company or its objectives	<i>aftermath</i>							
<b>Forgues (1993)</b>	– an event that causes, or may cause huge material and non-material damage, not excluding the owners and requiring immediate attention	<i>aftermath dynamics force</i>							
<b>Mitroff, Pauchant, Shrivastava (1988)</b>	– extensive damage and social disruption, extensive detrimental impact on people, the environment, important economic and social costs	<i>aftermath</i>							
<b>Lagadec (1991)</b>	– high impact adverse events with significant influence over the company	<i>aftermath force</i>							
<b>Weick (1988) Mitroff, Pauchant, Shrivastava (1988) Shrivastava, Mitroff (1987)</b>	– an event with a low probability of occurrence and far-reaching implications	<i>force aftermath</i>							
<b>Quarantelli (1988)</b>	– a situation that provides little time for reaction	<i>dynamics</i>							

Tab. 2.1 Overview of the definition of crisis – continued [67]

Author	Definition	Scene	Characteristics of the process approach			Characteristics event access			
			action	combination	transformation	particularities	surprise	startup event	origin
<b>Fink, Beak, Tadeo (1971)</b>	– organism (individual, group, organization, business) considers that it is in a state of crisis, if its set of model reakcii is unable to take a decision about the problem that caused the affected system	<i>aftermath</i>							
<b>Aguilera (1990) Slaikau (1990)</b>	– a situation that presents a dilemma in the need for a decision or opinion, which is crucial to change for the better or worse future state	<i>aftermath force</i>							
<b>Reilly (1993)</b>	– pernicious and destructive large-scale situation, which is a sudden and dangerous, requiring timely response, and that is not the typical operating course	<i>force aftermath</i>							
<b>Weick (1993)</b>	– cosmological episode that occurs when people suddenly and strongly feel that the world will no longer rational orderly system	<i>force aftermath</i>							
<b>Dutton (1986)</b>	– ambiguous situation in which the causes and consequences unknown	<i>causes aftermath force</i>							
<b>Shrivastava (1987)</b>	– random event turns into a crisis, they lose the ability to manage it	<i>force</i>							
<b>November (1984)</b>	– openly manifested in the transition from latent to acute stage of crisis development	<i>aftermath force dynamics</i>							
<b>Pauchant (1988)</b>	– a cluster of improbable events at the subsystem level or at the level of the system as a whole, which can potentially endanger more than one service, and thereby undermine the current or future operation of the system, which has a significant impact on the damage to the physical, psychological and existential level	<i>aftermath causes</i>							
<b>Roux-Dufort (1997)</b>	– a process that is running the event, which raises a series of accidents that individually have no reason to destroy and cause conflicts between family and other ownership interests. Crisis resulting from the sudden obsolescence terms of reference, an undertaking which temporarily or permanently destroys the ability of understanding, management and control unexpected events and has consequences that can affect strategy, the existence and behavior of members of the company and owners	<i>causes aftermath dynamics</i>							

**Tab. 2.1** Overview of the definition of crisis – continued [67]

Author	Definition	Scene	Characteristics of the process approach			Characteristics event access			
			action	combination	transformation	particularities	surprise	startup event	origin
<b>Pearson, Clair (1998)</b>	– business crisis improbable event with large consequences, threatening the survival of the business and is characterized by numerous causes, consequences and ways of addressing, as well as the belief that a decision must be taken quickly	<i>force aftermath causes</i>							
<b>Pauchant, Mitroff (1992)</b>	– disruption that physically affects a system as a whole and threatens its basic assumptions, self-perception and existence	<i>aftermath causes force</i>							
<b>Laufer (1993)</b>	– resulting from the erosion of common views, relationship building social and agreed mechanism	<i>causes aftermath</i>							
<b>Shrivastava (1993)</b>	– subversive urgency of the situation, with a decision reaching implications and restructuring of	<i>force dynamics aftermath</i>							
<b>Shrivastava (1987)</b>	– interaction of personal, organizational and technological failures in the business connected with the economic, social and regulatory failures outside the enterprise	<i>causes</i>							
<b>Shrivastava (1995)</b>	– transformation process stimulated a major disorder that necessitates restructuring involving social, human and natural systems	<i>force causes aftermath</i>							

The crisis is one of the **most challenging and the most fascinating disciplines of communication**. Information is rare, and often in times of crisis is not enough time for own surveys, evaluations and estimates. Although the experience can help, however, every new situation is unique and specific. Usually, there is no good or bad decision, a fast decision is required.

*The crisis is any situation threatening the integrity, reputation of the company or its relationships with key target groups, mostly caused by adverse or negative assessments in the media [49].*

The crisis represents:

- a condition that deviates from the normal,
- status, after which there may be a fundamental change in the monitoring process or activities,
- the status, which may arise as a result of the negative, but also positive information and the consequences.

Six essential features of a corporate crisis can be defined as follows:

- Enterprise often has less information about the problem than the counterpart.
- High interest to the public and the media about the issue.
- Surprising situations occur.
- Situation has unexpected and rapid development.
- Inability to fully affect the publicity on the topic by the undertaking.
- Managers and responsible workers suffer from panic and fear of further development.

To answer the question of whether an undertaking may soon find themselves in crisis is not easy, especially if the seeds of the crisis are considered. The trigger of the crisis can happen, for example, an error in the production, economic problems of the enterprise, a natural disaster, attack of the competitor and the like. The ability to detect and avoid all the crises, sooner than they break out, is the effort of most of the responsible managers.

The fact that an undertaking is in a stage of the crisis, can be detected by the very definition of a crisis, which represents the situation regarding the future existence and prosperity of the business. There is a decline in its credibility, economic prospects worsen, or very existence of the company is threatened the. Although each crisis is different, there are some common traits that are characteristic for the corporate crisis:

- someone is guilty,
- something is at stake (profit, and the reputation of the company),
- someone finds out something.

## **2.2 Typology of crisis phenomena**

The recognition of the state of company crisis is not sufficient to master it. It is necessary to identify the reasons the nature of the crisis and other required characteristics, that allow predicting the course as well as the possible measures to resolve it. The basic types of crises, according to the available views is given in Table 2.2.

**Tab. 2.2** Typology of crisis phenomena [67]

<b>Typology of crisis phenomena</b>	
<b><i>In terms of the frequency of crises</i></b>	
<ul style="list-style-type: none"><li>▪ <b>Disposable crises</b> that occur and solve them there after their re-emergence,</li><li>▪ <b>Recurrent crises</b> that are beyond solve them come back in greater or lesser intensity.</li></ul>	
<b><i>In view of the nature of the crisis</i></b>	
<ul style="list-style-type: none"><li>▪ <b>Crises caused by natural factors,</b></li><li>▪ <b>Crises caused by human factors,</b></li><li>▪ <b>Secondary crisis</b> caused by technological processes and devices.</li></ul>	

**Tab. 2.2** Typology of crisis phenomena – continued [67]

<b><i>From the point of view of the object, which reflects</i></b>
<ul style="list-style-type: none"> <li>▪ Crises in the economic sphere,</li> <li>▪ Crises in the public sector,</li> <li>▪ Crises in the environment,</li> <li>▪ Social crises, external and internal spheres.</li> </ul>
<b><i>In terms of the likelihood of</i></b>
<ul style="list-style-type: none"> <li>▪ Crisis with a high probability of formation,</li> <li>▪ Crises with a medium probability of birth,</li> <li>▪ Cross with low probability of occurrence.</li> </ul>
<b><i>In terms of the number of people who are involved in the crisis, or affected by it</i></b>
<ul style="list-style-type: none"> <li>▪ <b>Major crises</b> that affect more than ten thousand people,</li> <li>▪ <b>Medium duty crisis</b>, intervening thousand to ten thousand people,</li> <li>▪ <b>Mid crisis</b>, which extend to one hundred thousand people,</li> <li>▪ <b>Small crises</b> which affect ten to a hundred people,</li> <li>▪ <b>Crises individuals</b> that affect fewer than ten people.</li> </ul>
<b><i>In terms of out-plant crisis</i></b>
<ul style="list-style-type: none"> <li>▪ <b>Local crisis</b>,</li> <li>▪ <b>Regional crisis</b>,</li> <li>▪ <b>National crisis</b>,</li> <li>▪ <b>International crisis</b>,</li> <li>▪ <b>Global crisis</b>.</li> </ul>
<b><i>In view of the crisis</i></b>
<ul style="list-style-type: none"> <li>▪ <b>Sudden crisis</b> (immediate) – are the most feared, because they happen so quickly and unexpectedly that the exploration and planning left little time or no (eg. airplane crash, poisoning the product key executives death, earthquake, bomb attack or threat of attack a former employee of a firearm in the workplace). Sudden crisis requiring achieved prior approval of senior management with a general plan to respond to similar crises in order to avoid confusion, conflict and delay.</li> <li>▪ <b>Emerging crisis</b> (emerging) – give more time for research and planning, but can erupt suddenly after longer boiling point. This concerns for example of dissatisfaction and poor employee morale, sexual harassment in the workplace, substance abuse in the workplace, billing on state contracts and the like. Key to tackling the emerging crises is to convince senior management to take corrective action before the crisis reaches a critical phase.</li> <li>▪ <b>Permanent crisis</b> (sustained) – persist for months or years, despite all the efforts of management. Rumors or speculation come to the media, or spread with words, they can not be rebutted by means of public relations. Terms of reducing the number of workers in large enterprises, bribery of government officials, and the like.</li> </ul>
<b><i>In terms of the source of the crisis</i></b>
<ul style="list-style-type: none"> <li>▪ <b>In-house crises</b> are crises that affect the operation of the business. Are referred to as the crisis within the company. These include: <ul style="list-style-type: none"> <li>✓ material and raw material crisis,</li> <li>✓ crisis in manufacturing,</li> <li>✓ technological crisis,</li> <li>✓ financial crisis,</li> <li>✓ staffing crisis,</li> <li>✓ crisis know-how,</li> <li>✓ crisis management.</li> </ul> </li> <li>▪ <b>Out-plant crisis</b> relating to the external environment company. Indirectly affect the behavior of firms and their effect increases with the extent of the crisis and the toughness of the environment. Arise following out-plant crisis: <ul style="list-style-type: none"> <li>✓ crisis sales,</li> <li>✓ crisis deals</li> <li>✓ crisis of competitiveness,</li> <li>✓ crisis suppliers</li> <li>✓ crisis customers</li> <li>✓ crisis caused by a change in legislation requirements.</li> </ul> </li> </ul>
<b><i>In terms of the effect of negative factors on the ongoing processes</i></b>
<ul style="list-style-type: none"> <li>▪ <b>Creeper crises</b> that have their basis in the long oscillation around the steady state enterprise,</li> <li>▪ <b>Jump crises</b> that occur at regular intervals because of the action of the same factors.</li> </ul>



Tab. 2.2 Typology of crisis phenomena – continued [67]

<b>In terms of corporate crisis</b>
<ul style="list-style-type: none"> <li>▪ <b>Partial crisis</b> – hit just marketing, financial area, personnel area, and the like,</li> <li>▪ <b>Global Crisis</b> – affect all areas of the enterprise, the enterprise.</li> </ul>
<b>In terms of causes of the crisis</b>
<ul style="list-style-type: none"> <li>▪ <b>Natural crisis</b></li> <li>▪ <b>Technological crisis</b></li> <li>▪ <b>Confrontational crisis</b></li> <li>▪ <b>Malicious crisis</b></li> <li>▪ <b>Crisis caused by distorted managerial values</b></li> <li>▪ <b>Underwater crisis</b></li> <li>▪ <b>Crises subject to inappropriate behavior management,</b></li> <li>▪ <b>Business and economic crisis.</b></li> </ul>
<b>In terms of speed of the crisis</b>
<ul style="list-style-type: none"> <li>▪ <b>Slow growing crisis</b> that is caused by several dangerous occurrences and its accompanying feature is slowly decrease of corporate performance to the adoption of countermeasures</li> <li>▪ <b>Sudden crisis</b>, which is mostly due to one major event that seriously undermine enterprise.</li> </ul>
<b>In terms of the effect of the crisis on hold</b>
<ul style="list-style-type: none"> <li>▪ <b>Crises threatening the existence of the company</b> are either a minor threat, or provide enough time for action</li> <li>▪ <b>Crises are destroying the firm's crisis</b> with immediate manifestations of the crisis and are extensive.</li> </ul>
<b>In view of the possibility of prediction of the crisis and its consequences</b>
<ul style="list-style-type: none"> <li>▪ <b>Regular crisis</b> is predictable and can estimate its consequences. These are mainly technical and technological crisis, rarely on the social and natural.</li> <li>▪ <b>Unexpected crisis</b> is unpredictable crisis is sensitive to its effects. The emergence of the crisis is unpredictable and therefore can not make its prevention. It is important to ensure the improvement of information on changes that have occurred in order to prepare a rescue management.</li> <li>▪ <b>Uncontrollable crisis</b> has known danger area is easily identifiable in terms of location, time and type, but it is not possible to estimate the extent and complexity.</li> <li>▪ <b>The fundamental crisis</b> is the most dangerous crisis, because it is not possible to predict, estimate its manifestations or consequences.</li> </ul>

Depending on the nature of the crisis (Figure 2.1), they can be divided into predictable and unexpected crises. Unexpected crises often cause shock to the management, investors, government, media and public and represent the greater risk for the enterprise. To the predictable crises that are the result of a slow evolution of adverse events, the majority of businesses can be prepared and have also prepared contingency plans.

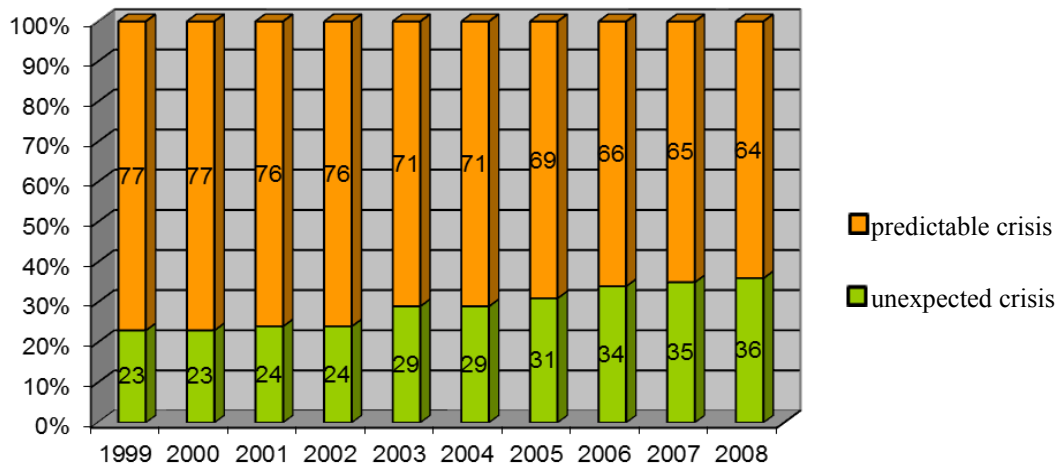


Fig. 2.1 Predictable and unexpected crises [4]

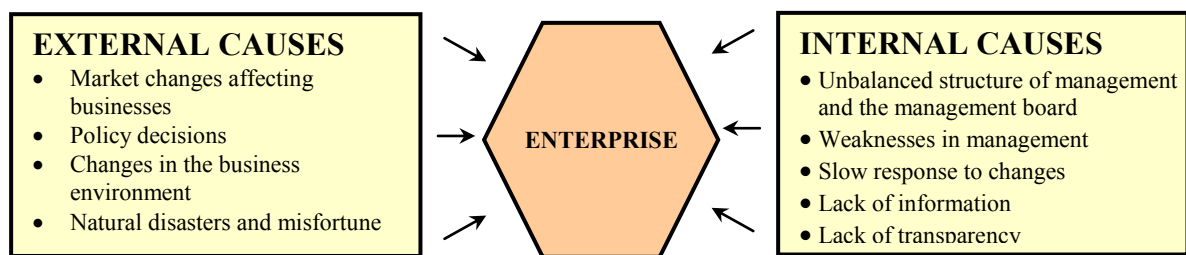
On average, over the past ten years, a third of the company's unexpected crises, caused by fires, explosions, natural accidents, violence in the workplace, and so on. The majority of corporate crises constitute a predictable crisis for which businesses they know rather than the public is aware of them. Management of the enterprise is able to prepare these and their progress is more controllable concept.

### 2.3 Causes of the crisis

Due to the constant changes in the business environment there is the need to manage and decide in unstable and information unsecured situations, which represent the **crisis phenomena** for the enterprise. The enterprise is provided with new conditions, which should be ready and able to respond in order to maintain the continuity of its existence.

In general, it is possible to divide the causes of the crisis phenomena in the enterprises (Figure 2.2) into two basic groups:

- **External, uncontrollable causes** that originate beyond enterprises and their development and progression can not directly affect the enterprise. Responsibility for these causes are carried by governments, central banks, courts, and the like. Despite the fact that some changes are very drastic, they do not justify the management company for their failure to cope.
- **Internal, influenced by causes** which are based on the internal situation of each undertaking. Under normal conditions, its nature could be influenced and eliminated. Direct responsibility for the failure to cope is carried by the management of these enterprises and to some extent also by the owners.



**Fig. 2.2** Causes of the crisis phenomena in enterprises [171]

The majority of businesses are still influenced by the combination of all the possible internal and external causes and it corresponds to the current status. The primary symptom of a crisis, such as a decrease in profitability, productivity and others are paid not enough attention and the crisis in enterprises gradually deepens.

The most common causes of corporate crises, according to the Institute of Crisis Management are given in Figure 2.3, where each of the crisis causes has been allotted a percentage of the total number of crises in the given year.

The most common causes of corporate crises during the last years can be represented by embezzlement, fraud, a class action and claims, as well as mistakes in the management of enterprises, or violence in the workplace.

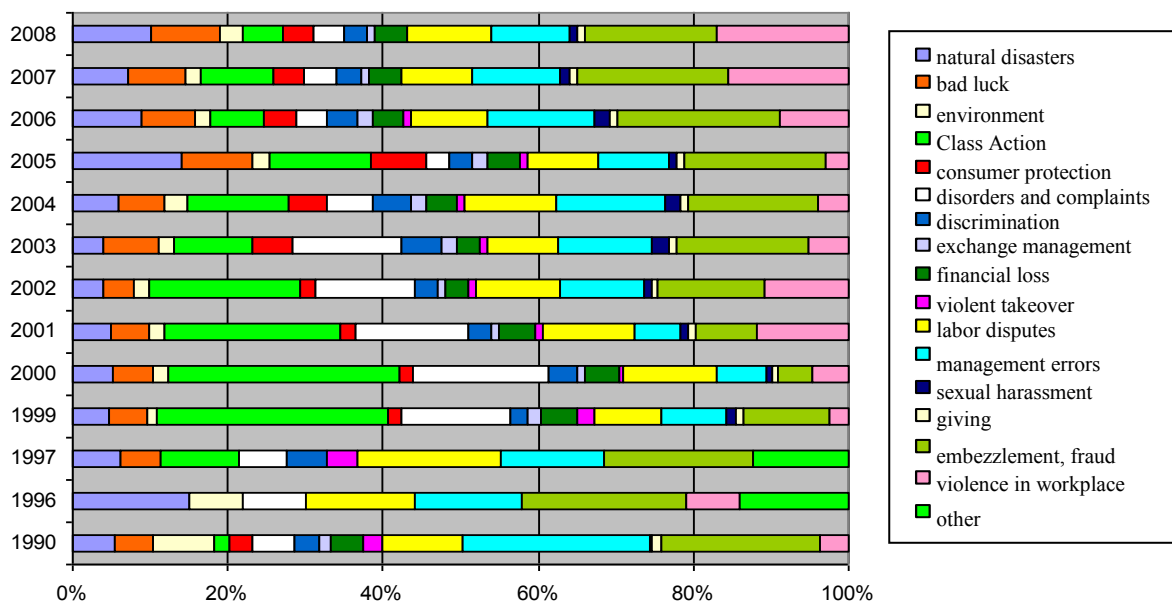


Fig. 2.3 Causes of crises in 1990-2008 [4]

The causes of crises change over the years. The most important changes in the causes of the crises in individual years are shown in Figure 2.4.

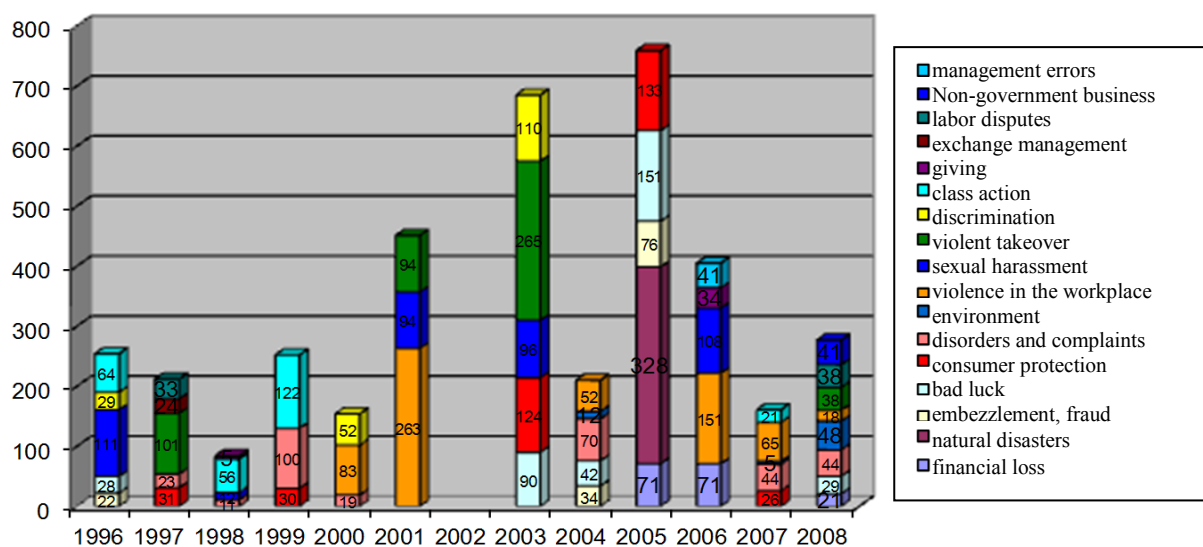


Fig. 2.4 The most significant changes in the causes of corporate crises during years 1990-2008 [4]

In 2005 the most important changes in the causes of the crisis were natural disasters, in 2003 violent takeovers and in 2001 violence at the workplace.

In the year 2008 changes in eight categories of corporate crises causes occurred against the previous year, higher than 18 %. Natural disasters have contributed to the formation of only 3 % of all corporate crises, but their number has increased year by year by 48 %, representing an increase of 305 corporate crises. The second most significant increase of 44 % was experienced due to disruption and complaints. The large increase in the years of 2006 and 2007 was due to the violence at the workplace, which in 2008 increased by 18 %.

Typical features of the enterprises functioning in Slovakia are:

- management shortcomings on the side of owners and managers,
- dominant autocratic management style,
- non-existent communicated shared values,
- minimum employee motivation and support of new ideas,
- minimum investments in human resources and management systems and personnel work,
- insufficient language training and information preparedness to new conditions after integrating the European Union [7].

From the above it follows that the outline for the creation of business crisis mainly the management and the staff are responsible, which is demonstrated also by the development at the global level (Figure 2.5).



**Fig. 2.5** Origin of enterprise crises [4]

The biggest responsibility for the crisis is carried by the management of the enterprise, that by its action and, often, inaction or ignorance contributes to the adverse development. The other group (Figure 2.5) comprises the factors such as natural disasters, the various technical and other problems.

## 2.4 Crisis as an event

Event approach to corporate crisis sees the crisis as a phenomenon that has a beginning and an end. A key feature is represented by the *surprise effect*, which occurs at the moment of the crisis origin, because the crisis is perceived as an unpredictable, uncontrollable and unlikely event. Crises are caused by an accident or coincidence, which represent unexpected events, as opposed to the routine, rules and experience. Crises are usually defined as *dangerous and harmful breaks*, often associated with extensive consequences that *threaten the overall survival of the company or achievement of its objectives*.

The crisis is *triggered by a specific event*, identifiable by time and circumstances. In the trigger event of the crisis is represented by the starting point of the crisis and, according to most researchers and professionals of crisis management, this point should be seen as the end point of a long process of destabilization within the enterprise.

The source of the crisis may be represented also by the *transenterprise causes* involving internal or external stimuli, based on social, personal, political, cultural, technical and economic aspects. The startup event is most commonly determined by the emergence of a number of mutually coherent phenomena, which occur in the period of "appropriate" conditions in the undertaking and its surroundings. The startup event of the potential crisis is testing the resilience of the business.

#### 2.4.1 Evolution of crisis in time

*The crisis, from its beginning to the end, goes through a time sequence of individual crisis situations that are continuous in nature and they largely represent the predetermined orientation of its further movement in time (Figure 2.6).*

Crisis chain helps understand the dynamics of the crisis in a particular stage of its development and allows us to respond to the problems of the crisis in times, in order to reduce the impact as well as to initiate original or new activities of the company as soon as possible.

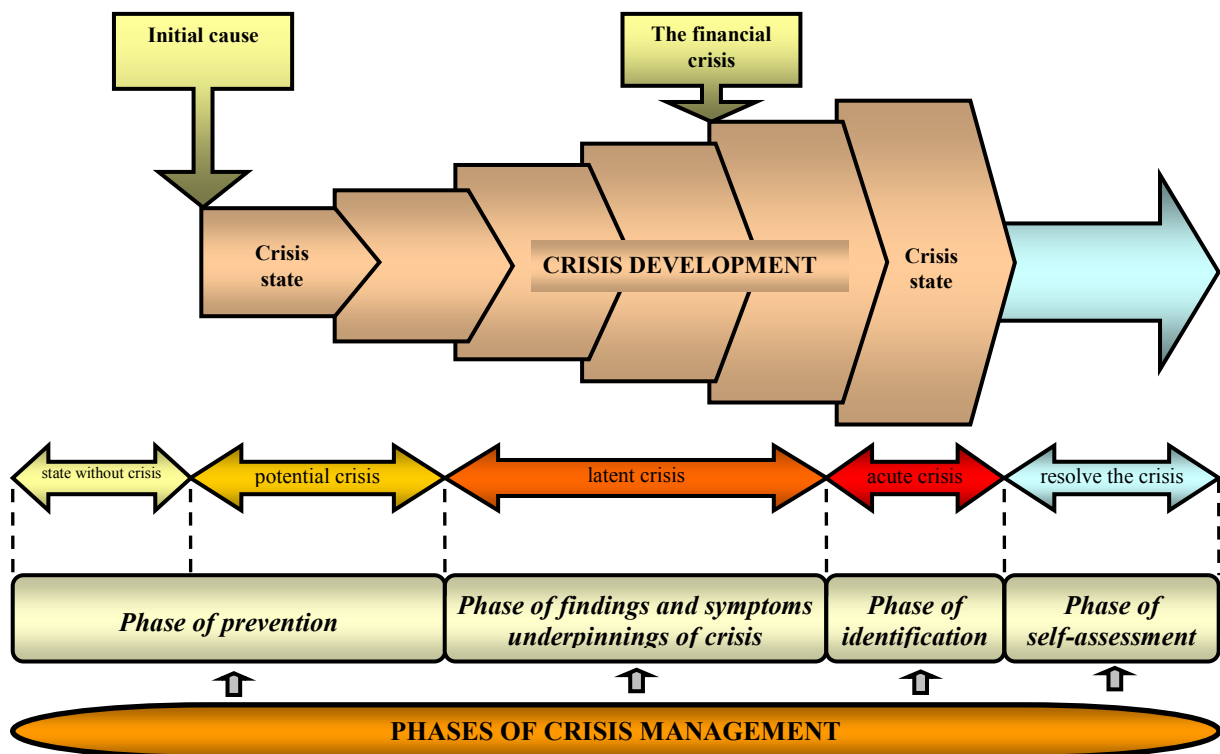


Fig. 2.6 Causal chain crisis [107]

Most of the crises in the enterprise, from their inception to destructive action, go through three stages, which can be considerably different over the time. The fourth stage is represented by solution of the crisis. Each stage of the crisis development is associated with the relevant stage of crisis management, which characterize the basic activities in the crisis stage given.

#### *Status without crisis*

The status without crisis is an ideal state, when a company has the high performance and its operation is effective. It is exposed to a variety of internal and external risks, which operate on its stability and efficiency. So far they do not represent risks for the enterprise.

### ***A potential crisis***

At the stage of a potential crisis, there are signs of instability and non-compliance with the planned course of the processes and their actual results manifested having various degrees of severity:

- **Slight symptoms of crisis** – are not observable by the general public, only to a narrow circle of specialists. In this period, it is difficult to make an adequate response and to prevent the spread of the crisis, because it is not possible to clearly determine the causes.
- **Weak signs of crisis** – partial information about the impending crisis, and ambiguous that only specialists in a given field of activity can identify properly. This period is very suitable for the use of an adequate reaction and removal of germs in the beginning of the crisis.
- **Strong manifestations of crisis** – more clear and comprehensive information about the impending crisis that can be properly evaluated by the majority of directors. After their findings, it is necessary to carry out adequate measures immediately, and with all determination.
- **Very strong manifestations of crisis** – complete and unambiguous information describing the impending crisis, which everybody can recognize. In such a case, there is a low possibility to an adequate response to the acute stage of the crisis, it is very complex, and the chance to avoid it is at minimum. However, it is likely that the extent of the damage and losses in the company can be decreased substantially.

Potential crisis is at its very beginning has many insignificant symptoms that are often overlooked by the corporate executives, as they can be detected only indirectly and often at random. Individual crisis phenomena appear first sporadically and only for a short time, then they gradually increase in quantity and power. If at this stage of the crisis beginning the sources of the crises are not diagnosed properly, increasingly intensive linking individual elements occurs. This leads to the accumulation of deeper causes of the crisis, which certainly picks up new causes and the crisis acceleration process starts. At this stage of development the crisis has the highest probability of success.

The weak point is the inability to anticipate future developments in the area of crisis situations of potential business, especially in the longer term. This limits the options to plan the development of scenarios and the risks and preventive measures. Experience shows that the use of forecasting methods for the reduction of uncertainty and risk are fairly limited and insufficient. It is therefore necessary to recognize the potential for the crisis to take the advantage of early detection of the crisis symptoms and make use of the flexible response to their findings.

### ***Latent crisis***

Latent crisis is the time when there is a discrepancy between the projected and the actual state of the processes is completely obvious and unique. The manifestations of crisis phenomena begin to appear. The basic functions of the business functioning are disrupted, threatening thus the very essence of the functioning of the enterprise. Therefore, it is necessary to immediately adopt special measures to eliminate already arising damage. Decisions are taken under pressure and with the absence of information.

Early recognizing and addressing the root causes of the crisis may prevent its further deepening and reach the balance. The crisis integrates the negative conditions of the previous stage, and deepens them. Remedial options, application of the elements and principles of crisis management increase over time, and the depth of the crisis is still limited. Solution to the crisis is associated with the negative impacts on staff at this stage, and social problems that require fundamental structural changes often raise.

Most commonly the latent crisis manifests itself as a liquidity crisis associated with the crisis of yields, which gets chronic in nature. Outages are common and lengthen, increasing thus the problems with sales, prices, buyers and sellers. The deviation from the original strategic objectives is studied.

### ***Acute crisis***

Acute crisis occurs when it was not possible to avert the crisis although using the measures adopted. A fundamental shift away from the company's development plans appears. The crisis may be a non-linear, can be re-graded. It brings the highest level of threat. It has a highly destructive impact on the overall business activity. The orientation of the production program is far from the needs of the market, as a result of underdevelopment no variable projects or production programmes are available. The enterprise permanently loses its clients and its market position deteriorates. The management and owners start to seek strategic measures, such as sale or merger of the company or its parts, and partial use of assets components in other business plans.

### ***Stage crisis solution***

The stage of the crisis solution is characterised by the acquisition of the balance in the company. Gradual implementation of the recovery strategy allows for the adoption of organizational, personnel, technology and other specific measures, which should contribute to the achievement of stability and new quality system [107].

## **2.4.2 The dynamics of the crisis in terms of its control**

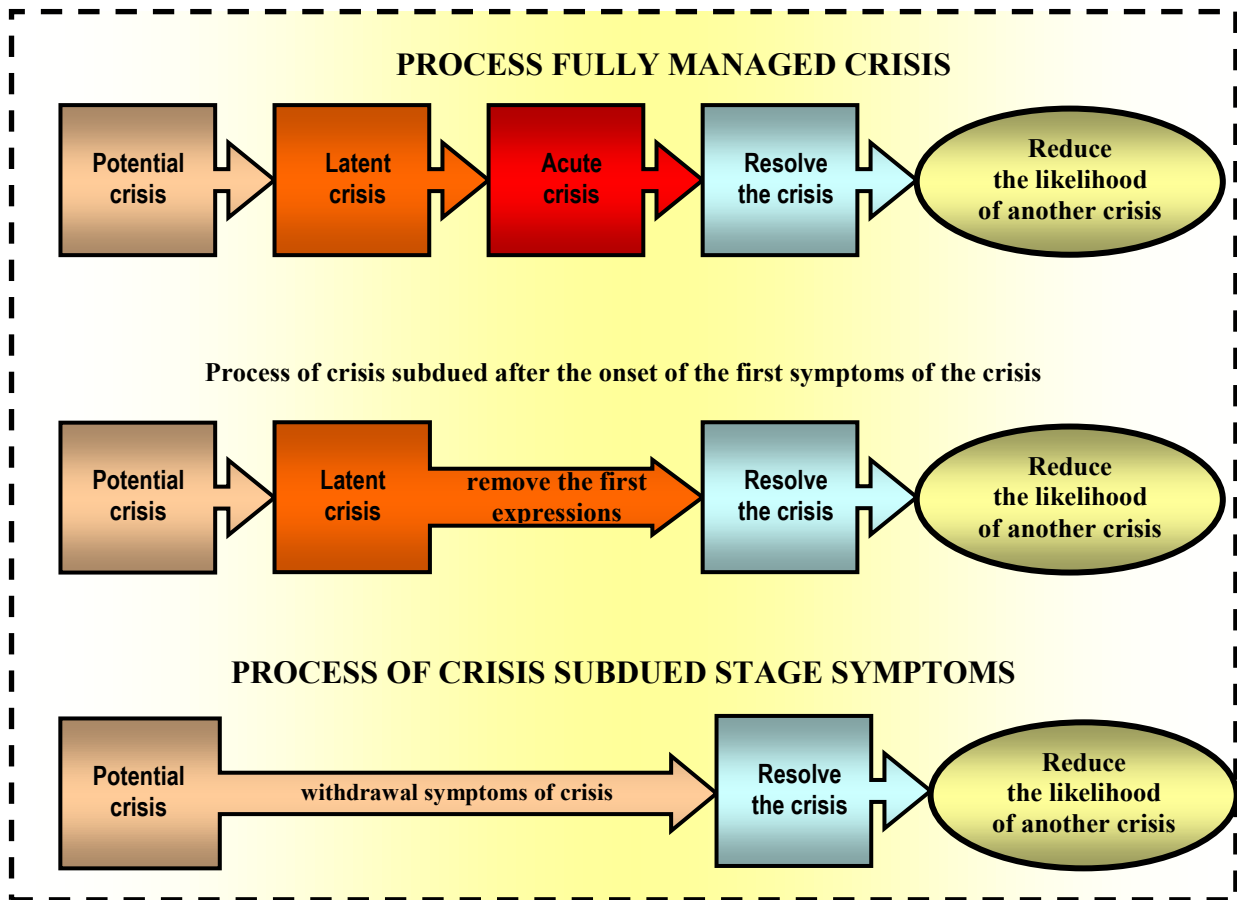
The corporate crisis dynamics represents the way by which the company settles the crisis down. For the crisis dynamics analysis are critical:

- **factors affecting the course of the crisis,**
- **sequence of the phases of the crisis,**
- **speed during the crisis.**

Every crisis has its particular development which is the subject of the crisis kind, its intensity, by which it hit the area, but also by the external and internal conditions in which it operates. The severity of the crisis may be the same throughout the period of its duration, or it can change due to the following:

- **measures adopted** – preventive measures before the crisis occurs, effective response in its course,
- **natural development** – changing the parameters of the crisis intensity in its course,
- **time** – every crisis is final, but the duration of the crisis may be, depending on its type and the conditions in which it takes place, very different.

Each crisis is characterized by a logical sequence of steps, which aim at the prevention of the latent and acute crises occurrence, or at least reduction of their negative environmental impacts. The course of the crisis can have three variations (Figure 2.7).



**Fig. 2.7** Variations of corporate crisis management [107]

Apart from the way in which the management of the crisis takes place, the damage and loss are reduced during each managed crisis as well as the likelihood of its recurrence. It depends on the level of understanding the crisis causes and the adoption of the optimal scenario for its solution.

For an analysis of the factors affecting the crisis course it is necessary to consider all the possible influences on the course of the crisis, assess their impact, and respect the mutual links and conditionality between factors, identify the key factors, and consider the possibility of exposure to these factors and their management.



**Tab. 2.3** Company crisis course crisis in terms of its control [55]

Type of crisis course	Graphic representation	Characteristic
<b>Ideal course of crisis in time</b>		<p>Crisis gradually through all phases of crisis development without skipping or omit certain stages. It is a model, an ideal course, which is rare in practice.</p>
<b>Unguided crisis with early end</b>		<p>Exaggerated effort to solve the crisis as quickly as possible may entail negative effects if:</p> <ul style="list-style-type: none"> <li>• not entirely clear causes of the crisis,</li> <li>• crisis is not completely under control and there are new symptoms,</li> <li>• are not comprehensively assessed the effects of actions taken to eliminate the negative aspects of the crisis.</li> </ul>
<b>Unguided crisis with slow end</b>		<p>The crisis, which occurs spontaneously or is eliminated random, unsystematic and non-professional bounds, or is controlled by an intuitive, tends to pass quickly and straightforwardly, and at the end of this process is succumbing to the crisis.</p>
<b>Course of fully managed crisis</b>		<p>Managed crisis can be characterized as:</p> <ul style="list-style-type: none"> <li>• crisis with overall shorter course,</li> <li>• crisis with a minimum duration and accelerated during acute stage</li> <li>• crisis with gradually reducing the risk factors during the acute stage,</li> <li>• crisis, during which stage of resolving the crisis than the swift.</li> </ul>
<b>Course of crisis subdued stage symptoms</b>		<p>The crisis is early detection, its causes are identified, process and methods of solution. Therefore does not reach maximum capacity.</p>

The length of the individual phases of crisis development differs during the crisis.

The state of crisis deepens up to that time, when the business ceases to be able to carry out its main tasks more frequently. First of all, the inability to abide its short-term obligations towards the suppliers occurs, later the undertaking ceases to be able to maintain the link to the development of supply and demand or the price development in the market, and in the next stage the longer-term obligations towards the banks, state or investors are threatened. If the fundamental solution to the crisis, its state and direction of development are not found, the business failure culminates bringing thus the decline.

Business entity stops its normal operation and liquidation of its assets in the form of covering its obligations to state employees, suppliers and financial institutions. The positive alternative is represented by the development – oriented and targeted effort to meet a specific crisis situation of the undertaking concerned with the fact that due to it the company gradually passes to stopping its further negative development towards the company demise, on the contrary it comes to its reversal in terms of restoration and further positive developments. It is a tool of crisis management, which is the active form of coping with the crisis, and the summary of such measures of the enterprise management enable the achievement of the objective given.

There are several ways in which the business can cope with an event that could trigger a crisis. Inadequate emergency response can provoke large-scale disasters, but also the proper reaction directed to the crisis with insignificant accidents can cause contrainuitive effects.

Some authors, such as Shrivastava, clearly puts event approach against the procedural one and states that: *"The crisis is not an event but a process extended in time and space."* In the event approach, the effects of the crisis work depending on their threats and negative consequences. In the process approach, the attention, rather than the consequences, pays a attention to the hidden risk factors and treats the crisis as a possible source of a positive change. The enterprise should be aware of missed crises. Crises cause changes and transformation at different levels of the enterprise. Change in the company will launch a sudden collapse of the basic principles and rules void in the company, which are then ineffective in addressing the crisis.

## **2.5 Crisis as a process**

Procedural approach considers the crisis in a wide range of time and space. Crises are seen as *a result of long periods of incubation and openly occur during the trigger events impact*. This is *the last moment of the continuing, cumulative process of corporate or organizational failures* [136]. Therefore, the genealogy of the crisis should potentially prevent the arising crises phase. Understanding the whole context of the crisis in the procedural approach, from the assumptions to the results, have to be primarily based on a systematic analysis of the crisis. The systematic analysis of the crisis management allows:

- reveal their dynamics,
- seek their historical roots,
- estimate the possible consequences for the enterprise.

The formation of a corporate crisis, according to procedural point of view, is inevitably caused by all three aspects at the same time:

- **Corporate weaknesses**, which represent an undercurrent and a breeding ground for the crisis.
- **Development of managerial ignorance** that makes managers blind to the presence of corporate shortcomings.
- **The startup event** of the crisis [136].

The first two aspects, corporate weaknesses and managerial ignorance, are a combination of two parallel concurrent processes. The main idea is to demonstrate that business shortcomings lead to the vulnerability of the enterprise if they are ignored or are not taken into account. Ignoring is not deliberate, but it comes from the gradual decrease of the human ability to recognize when the company imperfections grow into its vulnerability.

The procedural approach to the crisis provides a different perspective and points to the fact that the startup event is seen as a factor that reveals the previously existing dynamics of the crisis. In other words, what the event approach considers to be a crisis, i.e. startup, the procedural approach sees only as a amplifier of the process, which begins earlier, and the intensifies and accelerates the crisis.

It is not possible to do a lot to prevent or predict the trigger event in practice. On the other hand, the accumulation reduction of the previous corporate weaknesses and vulnerabilities, or reveal of these shortcomings represent aspects that can be influenced by the management.

### **2.5.1 Enterprise shortcomings**

Enterprise shortcomings are defined as significant *anomalies, errors, negligence, deficiencies, gaps created by an enterprise* or organization in conflict with management expectations. Any event in the company is considered a lack, immediately after starting to resist the managerial expectations and threaten the anticipated developments and laws that apply in the enterprise.

**The theory of enterprise shortcomings** says that businesses and organizations are imperfect units that generate a continuous stream of dysfunctions. The company imperfections are dealt with as a *side effect in the company's growth, movement, progress, innovation and development*. For example, industrial accidents do not arise only due to bugs in the system, but they are also the combination of serious failures occurring in all elements of the system. The likelihood of interactions of several local dysfunctions can be very high and can lead to even greater accidents.

According to the **Theory of highly reliable companies**, the businesses and are organizations understood as:

- productive and braking unit,
- result of the dynamic interaction between order and confusion.

The way the businesses develop and grow brings also internal and external shortcomings. External weaknesses reflect the effect of the production and consumption. Pollution, unemployment, health crisis reflect a kind of external fragility created during the development of their own companies. Internal side effects, sexual and moral harassment, violence and stress in the work environment, slander, gossip, conflicts that are part of an extensive grouping of hindering side effects of certain management practices, which may culminate in a crisis unless they are controlled timely and in efficient manner. The analysis of the business systems allows specifying the agents of the shortcomings, explain the complexity of the crisis and examine the layered nature of the crisis and crisis management.

**Crisis** in the process approach *is a natural part of business development and does not represent anything exceptional* [136]. It reflects the stage, beyond which the company is no table to exist any more on the same basis as before. The state of crisis in the company occurs at the moment of achieving the saturation by corporate shortcomings. Business shortcomings during their accumulation appear as different signals such as errors, failures, events, possible accidents, local triggers, active failures, unintentional deviations from the scheduled state, which can be interpreted as symptoms or peaks in the development of a crisis situation.

Individual signals of the crisis do not recall the company's response to their origin. Therefore, their continuation and cumulation, which, together with other events, systematically forms the environment suitable for the failure of the enterprise. The emergence of the crisis is mostly caused by a variety of historical, strategic and amplified, organisational and personal factors. The crisis is a phenomenon that via the increase and development of small events, is heading for a disaster.

Imperfections that arise in enterprises have different forms and sizes depending on their evolution. **The four stages are seen as manifestations of imperfections** and at the same time represent their level of visibility from the perspective of managers.

- **Anomalies** represent the lowest level of imperfections. They have the form of negligence, errors or any unexpected event associated with the natural evolution of the company. They are the result of natural variability in behavior and human undertaking. They are invisible until they do not jeopardize the enterprise or part thereof and are generally considered the part of the normal operating mode.
- **Weaknesses** are produced by a combination and accumulation of uncontrolled or poorly managed organizational anomalies. They represent a systemic vulnerability to adverse consequences of a trigger event and leave the room for danger. The weaknesses are sometimes considered latent failures. They act as complaints and reinforcing factors at the moment of the crisis start. Corporate and personal weaknesses are able to develop a crisis situation into chaos and confusion.
- **Cracks** arise when weaknesses reach the saturation level and the management loses control over it. They are considered crisis catalysts, i.e. triggering event. They are often described as dangerous offenses combined with an inadequate protection of business. They arise from the combination of active and latent failures. They are the result of a comprehensive set of interactive dynamic internal and external factors. The crack is the end result of the process of weaknesses accumulation, which is scattered throughout the enterprise.
- **Crises** are the ultimate stage of business imperfections. They reveal a whole series of internal latent failures, which are the main reason in terms of causing the events and their consequences. The most common critical indicator of external crisis is represented by media attention [136].

### 2.5.2 Managerial ignorance

*Managerial ignorance* is the second aspect of participating in the crisis in the company, it consists of the following perspectives:

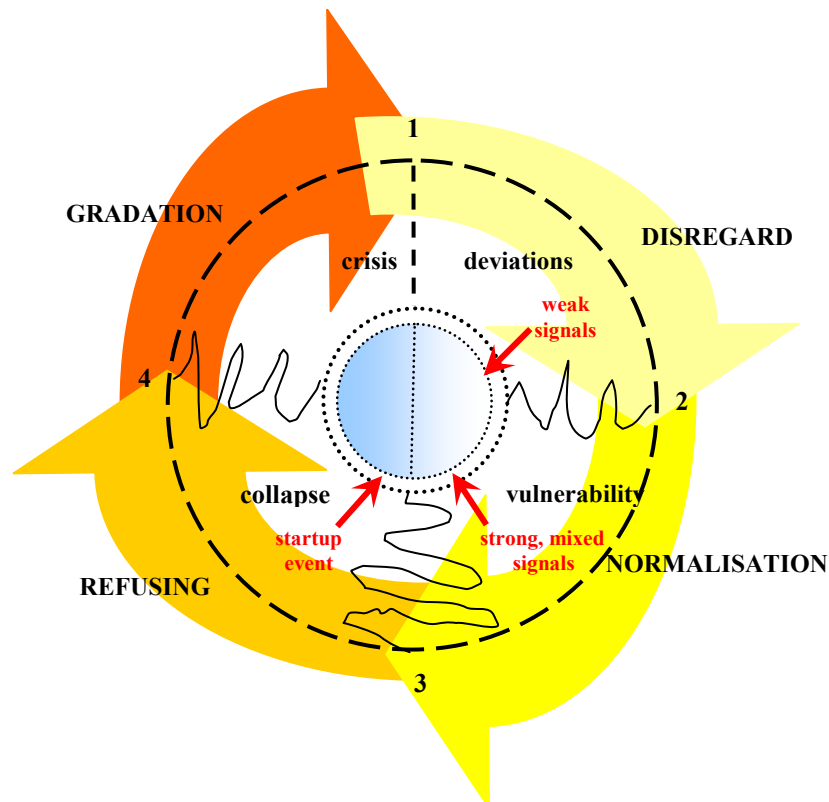
- **Psychological perspective** explains the occurrence of crises due to cognitive limitations, cognitive difficulties and prejudices that due to the fear from the reaction of the surroundings do not allow the managers to draw attention to events whose occurrence is unlikely and improbable.
- **The socio-political and cultural perspective** highlights the ignorance and rejection of warning signals and change them from unacceptable to acceptable risk levels.
- **Psychoanalytic perspective** explains the relationship between mental health and subconscious associated with the presence of crisis. It works with a group of existence, cultural and psychological defense mechanisms, to which an individual resorts to offset the lack of education and training in management. Crises are associated with the high degree of defensive behavior.
- **Psychodynamic perspective** of managerial ignorance is based on three conditions:
  - *Continuous search of self-esteem*, which represents the degree of alignment between the ideals of the individual and the current vision of themselves. The managers have a high sense of their organizational unit, which they attempt to protect and maintain, therefore, are sensitive to external reputation of the company, which they strive to protect from information revealing means. This need for self-esteem is regulated narcissistically.
  - *Atmosphere of turmoil*, which are increased by corporate shortcomings. The imperfections or controversial events increase the degree of agitation and may arise feelings of uselessness and disposal. They are the source of threat to self-esteem of managers because they create intolerant perception of the distance between the ideal and the actual state.
  - Used *defense mechanism to regulate the self-esteem*, which plays a critical role to explain the corporate deficiencies and maintains the managers at the stage of ignorance. The defense mechanism is any deviation from reality, which prevents to determine and remedy the mistakes done. To explain the process of the crisis the substantial defenses are as follows:
    - *Rationalization* is an attempt to provide for acceptable and unacceptable motives and acts carried out in the form of reasoning that is knowingly tolerated and acceptable. Managers, streamlining their past crimes, offer a retrospective in the protection of their own self esteem, striving thus to understand what has happened. Rationalization is the provision of suitable motives to justify their own inadequate decisions. The rationalization is close to standardisation. Normalization is an attempt to provide acceptable reasons and causes of unforeseen or unexpected events or actions and to usual deviations from the standards.
    - *Rejection* is simple and unconscious method to deal with an intolerable conflict, anxiety or emotional pain, which can lead to increased self-esteem and a sense of invulnerability. Managers deny responsibility for the failure to which they are exposed. Denial is a means to conceal the unacceptable facts from self and others in an unconscious effort to protect the self-esteem.

- The rejection is a means of trivializing the individual responsibility for controversial events. The rejection takes the form of masking the negative information, errors or failures, and developing arguments that deny the existence of imperfections or crises. An imperfection may arouse rejection because it uncovers potential inability to predict, plan and control.
- *Escalation of commitment* is a form of denial of reality and a reluctance of managers to admit that their previous resource allocations and decisions were inadequate. In the escalating commitment the managers receive a negative feedback response showing that they did not reach their target and therefore they tend to use other resources for achieving the objectives [136].

### 2.5.3 A procedural model course of the crisis

The following model of the crisis course is based on the procedural approach, which requires the development of a longer period of time comprising various stages of the crisis development. The model is divided into four stages from the deviations from the normal state, to the conditions of the crisis. The individual stages do not mutually exclude one another and do not represent the specific stages of the crisis evolution. The individual stages are intertwined and the shift from one to the next one is not direct and unambiguous, as shown in Figure 2.8.

The model works with the crisis as an overall process, and not as a traditionally understood phenomenon. The crisis is a process of inability to recognize the crisis as a result of the general growth of the enterprise imperfections and growth management ignorance, which allow developing of these imperfections up to the break-down of the business.



**Fig. 2.8** A procedural model of the crisis course [136]

Process model of the crisis course represents the connection of corporate imperfections and failures analysis with the mechanism of managerial ignorance and the most eagerly awaited and most characteristic defense mechanisms, which are characterized for each phase, where it is understood that *with increasing rate of corporate imperfections, that to a greater extent the managers use the mechanism of the controlled ignorance to protect their own self-esteem.*

### ***Stage 1: Deviations from normal and neglect***

In different areas of the enterprise **small deviations** origin which are minimal and generally insignificant. Disorders may sometimes generate weak signals that do not have sufficient potential to create the awareness of managers. The managers automatically do not register a small deviation and even when they register, they do not pay enough attention to them, because they do not assign them the importance needed.

The first stage represents the way managers work daily with the standard flow of information and events. Uninterrupted flow of information and events does not leave enough time for decision making. To work with information managers use methods to facilitate the work, such as tolerating errors, filtering and generalization. The systems of processing analysis and information are implemented, which automatically control and select information. The managers resort to a small defensive routine, known as purposeful neglect, which is associated with the situation, in which some previous knowledge, response and expectations are required for a quality decision. *Limited capacity of knowledge reduces the ability of the managers to develop a concept of variations in the company and allows them to remain in their previous expectations.*

### ***Stage 2: Vulnerabilities and normalization***

In the second stage the imperfections gain via its accumulation larger dimensions and overreach the **vulnerability of the enterprise**. Individual conflicts arise, the strikes continue, as well as the adverse articles in the newspapers, there is a loss of company privileges, which had an increasing number of complaints from customers, resulting in the loss of important contracts, repeated quality problems, there is a high staff fluctuation, and so on. These events, act as a warning, and sometimes as a precursor of potential dangers, which provide stronger signals for the visibility of the potential risk in the enterprise.

*The signal of the potential risk is represented by information that deviates from the expectations and challenges the existing view of the world. This is a strong signal. The signals are mixed, because once the information indicates a problem in the company and immediately after it there is a new piece of information indicating that everything in the company is ok.*

Variations in the business have a high degree of visibility, however, they fail to arouse the sufficient attention of the managers, because they are still unambiguous. The risk signals in the undertaking find the expectations of managers, test their ability to disrupt the patterns and foreseeable development of the company and potentially change their ability to work with the results of the company. The degree of anxiety in the company increases. *At the moment, if the vulnerability of the enterprise becomes visible and in exceed the certain degree of laws and the foreseeable company development, the warning signals occur and the managers approach the rationalization to strengthen their expectations and reduce the degree of anxiety.*

If the managers repeatedly face the unmanaged warning signals, the rationalization takes the form of **normalization**, which is represented by the acclimatisation of the company imperfections and deviations. *If managers repeatedly encounter the signals of vulnerability, they consider them as part of business stability and normalize their alternating presence.* The anomalies and vulnerabilities are subsequently considered as suitable conditions for the success and efficiency of the company.

An alternative way of looking at the second stage is to regard the managers capable to correct potential incidents associated with the company vulnerabilities. If the incidents are managed successfully, without removing the essential vulnerability, the company's potential for the emergence of danger will persist, yet the managers acquire the feeling of control and own invulnerability. The false feeling of control over the unexpected events provides the managers with the feeling of success over the control of the existing situation and became convinced that they are able to control any similar adverse situation that may arise in the future.

*If the managers can successfully handle the incidents generated, they experience the feeling of its own success and growth, which support their unreasonable feelings of control over other unexpected events, regardless whether they are able to remove all the causes of the enterprise vulnerability thoroughly.* During the second stage the company's problems are often dealt with via normal processes or random management practices.

### ***Stage 3: Collapse and denial***

The transition to the third stage is marked by the transition to the company crisis. There is the occurrence of an event which is more important than all the previous ones, and which frees the vulnerabilities, which have hitherto accumulated and combined with each other. There is a total collapse of the activities and organization of the business. As a result of the **collapse** it comes to the disruption of the order, traditional values and beliefs established in the enterprise. There is a radical distortion of expectations, destabilization and the explosion of traditional values.

Solution to an existing negative situation of the enterprise is connected with the emergence of the shocks, and the ability to control the panic is temporarily limited. The survival of such an event, as the crisis definitely is, can cause the psychological breakdown, undermine the values and the self-confidence of the employees and managers. The emergence of problems in the enterprise is dynamised by the time and it comes to the lowering of the ability and narrowing of the space for an adequate response. The third stage of crisis developments in the business, in contrast to the two previous ones, is very short, fast paced and intense. Therefore, to understand the causes of the crisis and maintain the overall problem the managers overview what is happening in the business. The managers often experience the disillusionment, the feeling of helplessness and confusion. They may lose their sense of values and control.

Commonly used management practices are inadequate and unsuitable for the satisfactory explanation of errors in the management. On one hand the interconnection of the various vulnerabilities requires from the managers to apply creativity to solve problems, and requires, and on the other hand, the enterprise is required to accept the proposed measures. The managers repeatedly resort to their own defence mechanism, in order to justify the traits and signals of potential risks and they resort to the rejection of reality. *In the period of serious problems at the company, the managers temporarily deny and reject the reality to retain the ability to act and the ability to resume control over the emerging problems. Their reaction is*



*to call for speeding up the course of the crisis, thus restricting new errors and accusation.* The attitude of rejection can be coupled with the insults and accusations of others, or even with the refusal to admit any responsibility for what is happening in the company.

#### ***Stage 4: Crisis and growth of responsibility***

After the stage of collapse there is the stage of the **crisis**. The collapse of the company starts mutual combining and amplifying of long collected internal vulnerabilities. The trigger of the crisis may be represented by internal or external causes. The enterprise and its structure is compromised and the company may slip into a deeper personnel, social, managerial or other crises. The managers face a complete destabilization of the enterprise and its environment, standing right in front of the issue of resolving the crisis, their position in the company is at risk.

The managers attempt to avert the existing unfavorable situation, they would likely implement such actions that convince of the own involvement in solving the crisis. Helplessness and inability to solve the existing problems caused by the crisis creatively, it forces the managers to apply known procedures, or use learned behavior, and thus reproduce the already tested solutions. *In the period of the crisis the managers show a growing suspicion to possible inappropriate responses based on previous experience or behavior,* thus trying to save own self-esteem and apologize.

During the crisis aftermath the managers slowly realize that the company cannot be managed the way it was before the crisis [136].

### **3 CRISIS MANAGMENT IN THE ENTERPRISE**

Crisis management is a systematic response to unexpected events that threaten people, property, as well as financial and operational stability of companies. In a turbulent business environment the crisis management becomes an increasing part of routine management work.

In a broader sense, the crisis management is a control tool designed to cope with a crisis situation. Perceived classically, it begins by identifying the company crisis potential and continues by setting the processes of crisis prevention, next by the action and efficient management of the crisis and ends by the elimination of the crisis consequences. According to the procedural approach the crisis management represents a still present and never-ending process of corporate control of companies, which is the part of business management.

The basic feature of the crisis management can be represeneted by the low possibility to predict the future events, and the need for rapid adaptation to changed circumstances. The crisis management constantly works with the critical negative effect on the company functioning as well as on its employees, then it works with the psychological stress and critical attention of the company business partners, competitors and social surroundings.

#### **3.1 Role and position of crisis management in the enterprise**

*The crisis management is the summary of control activities of the crisis management focused on the analysis and evaluation of risks and threats, planning, adoption of preventive measures, organizing, carrying out and control of the activities carried out in the preparation to the crisis situation in the enterprises as well as by their solutions.[63]*

The crisis management represents the management of business operations during the company crisis in the extent, in which it is possible to manage such events. The crisis management is also represented by a series of measures to minimize the potential for damage resulting from the crisis. It is efficient, both in preventive elimination of the possible crisis as well as in coping with the crisis. It is built on two pillars formed by:

- plan of crisis management,
- plan of crisis communication.

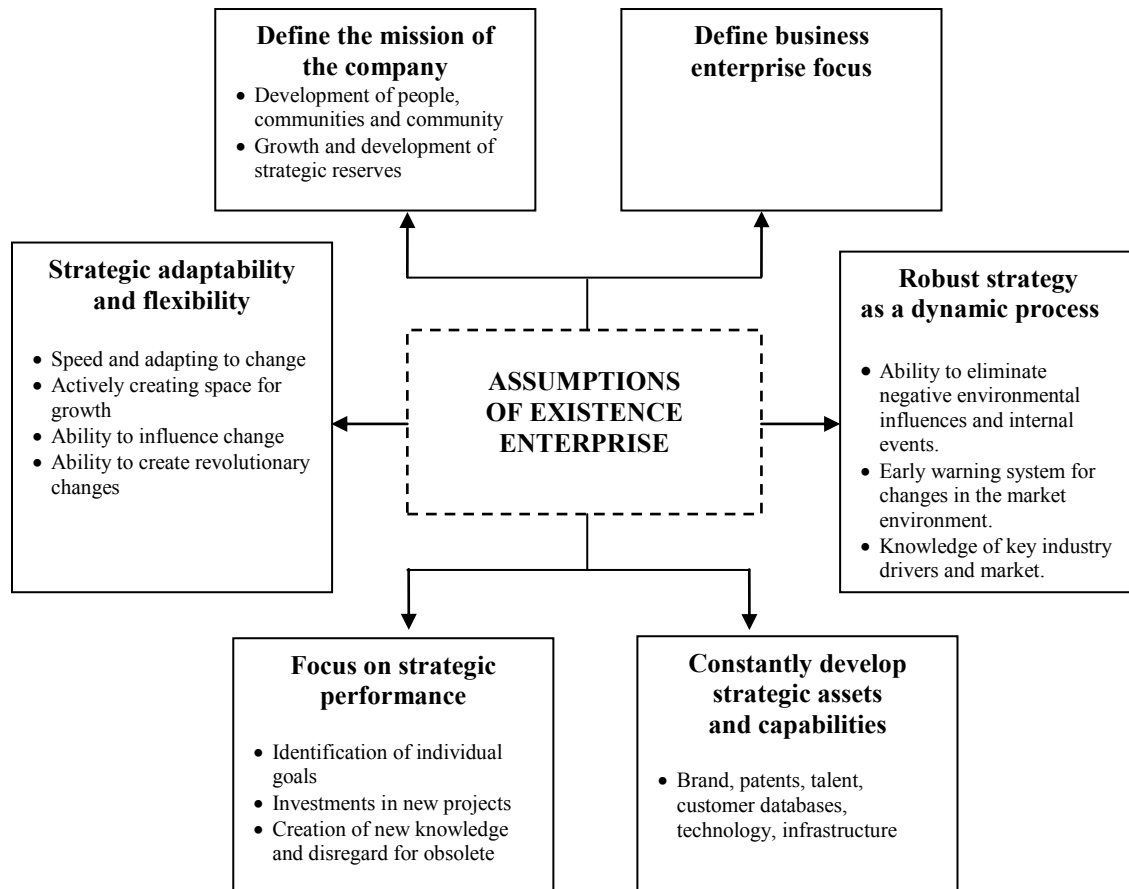
The crisis management is not a set of mechanical rules, procedures and activities, but a set of sophisticated processes and the successive steps aiming at the prediction of the complex nature of the crisis. This substance, depending on the point of view, has its real, but also its perceived form.

In general, the crisis management has **four objectives**:

- reduce the tension during the crisis event,
- demonstrate corporate commitment and expertise,
- control the flow and accuracy of information,
- manage resources efficiently.

The crisis is one of the conditions inherent to the life-cycle businesses, therefore, it is essential that the company has the managerial structures able to handle such situations. That

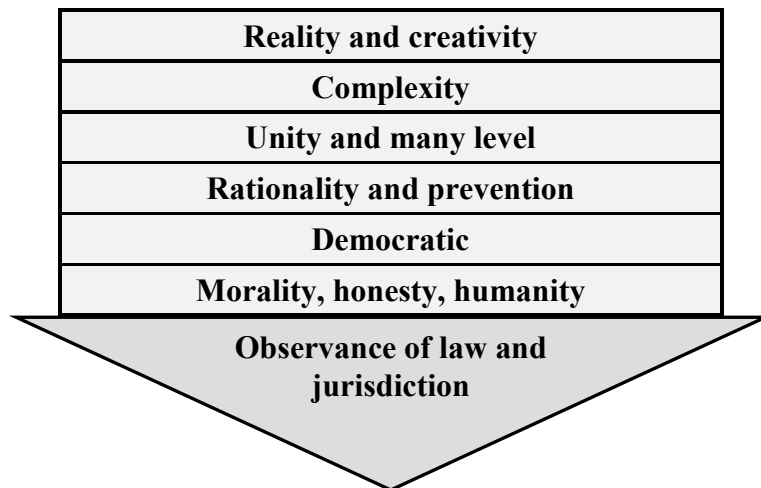
is, that the ability to handle the crisis, or manage the elements of the crisis management belongs to **fundamental responsibilities of manager** and the training for that qualifications should be a part of all structured management training programs.



**Fig. 3.1** Prerequisites of enterprise existence

There are extensive restructuring and redevelopment projects, which require the active involvement of the managers, for who the crisis management is the key qualification. This is related to the question of the continued existence of the crisis management in the company, which has already mastered the crisis: after the crisis such a company needs a strategic impulse that steers it to the further development and the presence of the crisis managers in the company seems to be counterproductive.

Management techniques necessary to manage the crisis management are inherently different from those necessary ones for the dynamic development of the company. If the crisis manager can brilliantly manage and deal with the crisis, it does not mean that s/he can successfully manage the company stabilization and development stages. The crisis managers need the crisis for their professional lives in order to train. If there is no crisis available, a the crisis manager should create such a crisis by him/herself. In practice, this means that the crisis manager still acts as s/he is used to the times of crisis. S/he applies the dictatorial approach, refuses to delegate the authority and does not operate in favor of the release of creativity and creative potential workers at the slightest, which constitutes an essential imperative for successful business development. The implication that the same manager who can handle the demanding crisis management has to cope with the seemingly less ambitious stabilization and development management.



**Fig. 3.2** Main features of crisis management

The crisis management in the course of time, has transformed into the scientific discipline, which is part of study programmes in a series of economic and management tutorials-oriented colleges and universities. For the managerial procedures in emergency situations empirical techniques are derived, while some of the recommendations are close to the normative models. Individual authors, however, are more or less unified when considering the crisis management procedure:

**Anticipate the crisis situation** and consider the possibility of a potential crisis situations. Prepare for these situations and perform quality audits to analyze these activities.

**Create plans for crisis measures** as an integral part of business planning system under the conditions of risk and uncertainty. The crisis scenario may become a direct part of the corporate strategy prepared with alternatives. For the successful survival of the crisis situation an emergency plan is suitably formulated. In this context, it is interesting to note that currently less than 30 % of U.S. companies have efficient contingency plans processed.

**Use transdisciplinary teams** composed of qualified staff to deal with crisis situations. There must be a real and formal support of these teams by the management.

**Ensure the information processes** for the implementation of sequential and parallel management functions in resolving the crisis situation.

**Ensure** the internal and external **communication** with relevant stakeholders.

**Ensure the consistency** of recovery objectives with the corporate strategy. The key is to switch the strategy early into the crisis scenario.

**Perceive the interdependence and conditionality** of crisis factors and propose corrective measures to respect and emphasize the complexity of all the measures.

**Cope with the psychological demands** of the crisis management during the crisis and after the crisis is resolved or gone. In the implementation of emergency measures it is necessary to proceed up ethically and analyze the possible impacts of the adopted measures on corporate culture and company image.

**Identify and exploit the positive aspects of the crisis**, to which the following phenomena belong:

- crisis as an incentive to innovate,
- crisis as a business opportunity.

The potential of leadership and talent of some involved workers can be revealed as a part of the crisis positive effects.

**Cope with crisis communication** means to have a clear target orientation and responsiveness to effective management in the times of crisis.

**Maintain the proper sequence of steps** of the crisis management, which include:

- appointment of a crisis management team,
- evaluate possible crisis development scenarios,
- development of a formalized crisis plan and its continuous refinement,
- periodic training of crisis situation solution,
- respect of the crisis communication principles.

The parallel between the crisis management in the business world and the conduct of military operations is illustrated by Major General William A. Cohen in his book "The New Art of the Leader." He applies the winning tactics of a military leadership to the subject of business. The approaches are documented by the examples of real operations in the Persian Gulf and Bosnia and at the same time he confronts the uniqueness of leadership personalities from the military and business world. The recommendations to manage and control the crisis situations are summarized in seven points:

- Quickly set out a set of objectives that are understandable to all.
- Appropriately communicate their intentions, procedures of negotiations and achieved results with employees and retain their attention.
- Acting boldly with the necessary courage, not fear the eligible risks.
- Be decisive and not to avoid unpopular measures.
- Operate and dominate the situations, retain the initiative and not be drug by the event.
- Act exemplary and ask the others to follow the leaders.
- Not hesitate in choosing the necessary new colleagues and get rid of unsuitable ones. Act wisely in order to minimize the risk of error.

### **3.2 Most common deficiencies of the crisis management**

Common mistakes that businesses and their managements commit in the crisis management are summarized in the following points:

#### ***1. Individual fields of management are not controlled in their contexts***

The communication is the foundation of cooperation. In enterprises, where the cooperation and coordination among the various departments and services does not belong to the management priorities, the risk management cannot work well. The variety of problems and potential failures should be dealt with in isolation and on the basis of partial information. This results in the conclusions with a very limited effect. The proposed measures cannot be too efficient, and then sometimes they are directly counterproductive.

#### ***2. Insufficient attention paid to mutual interactions of processes and risks***

Consequence of the absence of a systematic approach is a frequent tendency to explain the shortcomings, failures and accidents by the partial causes, usually by the technical or factual errors of people and often also by random influences. It is forgotten that the ignoring of interprocess links leads to isolated decisions and measures and new risks.

The basic premise of the active risks prevention is represented by the implementation of the systematic analysis of the interactions between the deviations from the optimum during the process. And even those ones which may be insignificant, but in combination they gain a potentia, by which they may cause serious disorders of the main processes.

***3. Concepts of internal customers and owners of the processes are not applied adequately***

Each worker needing the results of the work of another worker for his/her activities, has the right to get them in the required quality and in a timely manner. And similarly, s/he has to meet his/her obligations to other customers, and processes. Otherwise, it becomes a brake to the entire process and bears the risk.

***4. Systematic processes identification and risk assessment are not carried out***

There is an underestimation of the methodological training and comprehensive monitoring of risks. It is s verified by experience, that the omission of a single significant risk may depreciate the results of the analyses carried out, as well as the subsequently applied measures.

The identification of processes is the part of the crisis management and must be followed by the search, evaluation and optimization of factors, influences and conditions that affect the reliability of the process. Everything is used to implement effective corrective and preventive measures.

***5. Insufficient focus on the identification deep casual risks and failures***

Every failure is the result of deeper causes, because the aim of a risk analysis must be represented not by the symptoms, but the deep causes. Preventive measures that are not based on an analysis of the causal chain of causes and effects and on the disclosure of deep causes are generally ineffective.

In general, the methods used for the analysis of risks, suit only little to the complexity requirement. The usefulness of the results obtained always depends on the skills, knowledge and experience of the evaluators. It shows that the investigation conclusions often tend to be one-sided and that not the actual causes but their consequences are considered to be the sources of events.

***6. Insufficient or improper management of human factor performance and reliability***

One of the axioms of the risk management is that every failure process is primarily caused by the human component of the system. If a thorough analysis of faults, failures, accidents or other adverse events is done, it is always finally revealed that someone directly or indirectly involved, performs a wrong operation. Further investigation has to find why such a failure has occurred. In general, that for every human error the long-term existing and overlooked causes can be found. The human factor failure is the only a symptom, i.e. the result of some other, deeper and rooted causes. The result of an investigation has to answer two questions:

- Who, at what stage and in which processes prevented not the unwanted event, who allowed it or even directly caused it?
- What factors together meant that a person failed in carrying out activities?

The rule is that if the human failure is not detected, the analysis was not performed correctly and sufficiently.

***7. Tendency to prefer the implementation processes at the expense of source processes***

The principal tasks of the management include the identification of processes which are implemented in the company and meet their objectives. These processes are described by the term of implementation or major processes. Every such process must be adequately implemented and managed and must be supplied with the necessary inputs and resources. The management terminology distinguishes also the supporting or auxiliary processes. The concept of the process management is based on the fact that the so-called supporting or auxiliary processes providing the resources necessary for the function of the implementation processes are of the primary importance for the effective implementation of products. Their significant part must be implemented before the implementation processes can be run.

***8. Insufficient emphasis on proactive approaches***

Management knowing where it is going, differs from others in that it has the corporate goals formulated and announced. In management terminology this means that it has processed the enterprise mission, policies and strategies, that it has to build the system of monitoring the meeting of the objectives and risks that may threaten their performance. Such management may be marked as proactive.

The role of the proactive analysis is to obtain information for timely and effective prevention of procedural failures. The proactive approaches are the opposite, as well as the complement to the commonly applied approaches that focus exclusively on the analyses of reactive disorders and accidents that have already occurred, with the aim to propose the measures to prevent their recurrence.

***9. Poor culture***

Effective processes of the corporate culture development should be a priority in any business, and should be dedicated daily attention. The same is true for the culture of safety, communication, interpersonal relations, which are an integral part of the corporate culture.

The corporate culture has a large influence on the attitudes of staff towards the crisis management and risks themselves. The key positions include the awareness of accountability, which is immediately shaped by the corporate culture. At the same time the most important pillar, on which the corporate culture is built.

The management tasks include also permanent increase of the crisis management prestige and process reliability and security in the corporate environment. Certain pressures and positions, such as the plight of the senior management preferring the economic targets in some situations to the risks prevention to contribute to the bad situation.

***10. Insufficient support of projects and processes of changes***

The solution of enterprise crises is associated with the business changes and the emergence of new risks. The management of changes is therefore one of the key features of the corporate management and at the same time one of the most important management skills.

The crisis management has to be able to monitor the ongoing changes in the company. It has also to identify the need for changes, promote them and manage their implementation. The attention and support given to the change processes and projects must be effective and visible. For the success or failure it is critical to persuade the people to accept the changes and their implementation. The frequent shortcomings of the crisis management are in particular areas such as process management, communication, change, environment, culture, development of the necessary individual and team skills, knowledge, skills and attitudes.

### **3.3 Crisis manager**

Similarly as every business is original, every manager is original. The uniqueness of the person brings to the managerial position an added value. The manager it should never give up, or copy anyone. Only the most experienced, only the people with moral values, are able to take their power with humility, understand that they do not become indispensable or infallible, that they cannot do anything, that they are obliged to bear the responsibility for all who will follow.

- **Can work with others** – The manager is not lonely runner and his/her ambitions can be satisfied only via a team. The manager of 21 century has to the control rules of the customer orientation, the area of added value, as well as dealing with people as with the competitive advantage, and this all using the information technology.
- **Has universal knowledge** – Degrees, certificates, diplomas from prestigious universities are essential, but no guarantee of managerial success. The competition intensifies over the years, opening of the global markets raises new challenges to the managers. The competition is threatened by the ability to do what is needed to be done and just now.
- **Knows what and how to do it** – A successful manager depends on successful personal relationships. Informal, relaxed and friendly style of communication with people is the assumption that the right information reaches the right people at the right time. The crisis manager uses comprehensive words, skilled and prepared speeches, efficiently calls and chairs the meetings, has the ability to negotiate with the result "win – win" and the ability and willingness to listen to others.
- **Self-development** – Many crisis managers are convinced that now it is not the time for further education. They believe that their primary and sole mission is to act, and that education is useless, but a distraction. They are constantly busy and under time pressure. Nevertheless, the position of the manager has the requirement of the permanent development and self-learning high on demand. Today, it is no longer rare, that the doctoral study is not only the basis for the academic career, but also a thorough training of a manager for challenging positions in the managerial practice.
- **Own development** – Systematic study of foreign languages, knowledge of business issues in the European area, the orientation in the global issues, and a general overview of the situation in the field and the nearest business environment, these are the essential prerequisites for the success of a crisis manager. The manager has to interact with its environment in the sector, but also beyond it.
- **Verified in practice** – The personality of a crisis manager is based on the active participation in professional and other expert associations, participation in various projects, but also by the active performances on seminars and conferences and publications.
- **Versatile personality** – The manager of 21 century is endangered by too much work, loss of privacy, inability to relax, a strong focus on goals absorbing their meaning, and physical and mental problems.

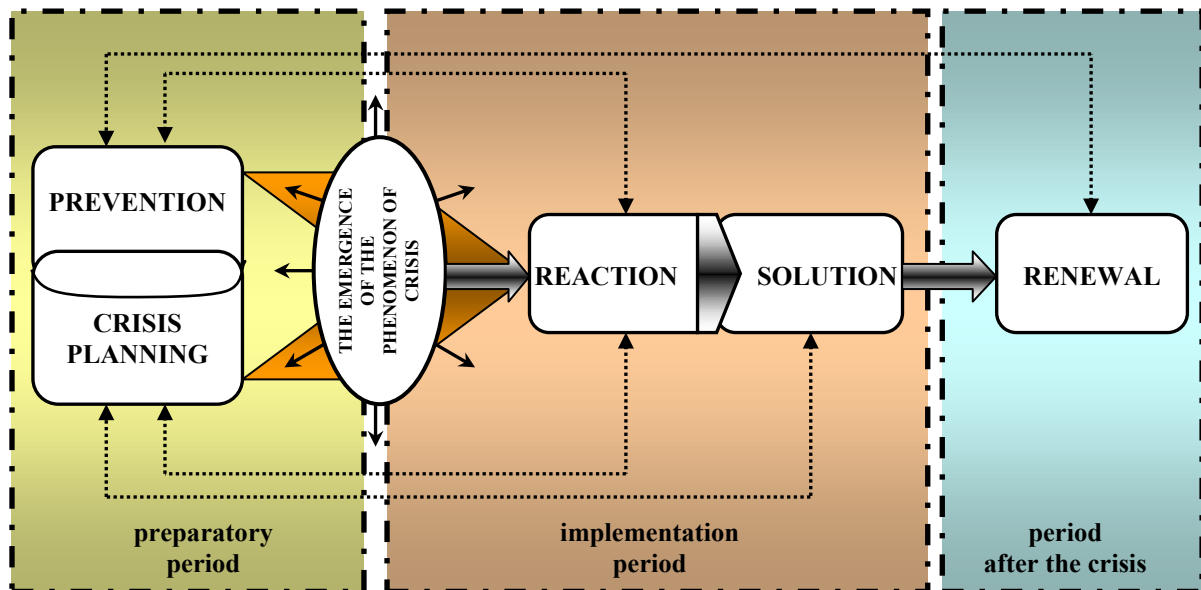
It is necessary to adhere to the mental hygiene, alternate the work with rest and not leave the matter to itself, "it will develop somehow", s/he has to organize the rhythm of own life. The premise is to ensure the quality of preventive health care, the building of the group of friends with whom s/he can communicate openly and does not neglect the private life.



- **Pleasant companion** – Career is a lifelong process, inseparable from personal and professional development. The managerial position includes a number of challenges, incentives and opportunities to fulfill personal ambitions at one's best. It requires a lot of energy, sacrifice, perseverance, understanding and enthusiasm.

### 3.4 Models of corporate crisis control

The crisis management deals with the crisis phenomena in the particular time and in defined stages, which can be described in detail and the links can be explained. The basic theoretical model of the crisis management is given in Figure 3.3.



**Fig. 3.3** The basic model of crisis management [107]

Stages of prevention and crisis planning intersect. The more complex and more effective prevention, the less extensive contingency planning must be. The absolutely effective prevention prevents the occurrence of crisis and the crisis planning loses its importance. The immediate and effective response to the crisis is a tool for reducing the damage and losses. The system restoration is not only the task of the crisis management. Crucially, a legal person that has been damaged or threatened by the crisis, has to participate. The crisis management has to evaluate the course of crisis in detail and adopt conclusions to modify the preventive measures also for the crisis planning.

The individual components of the basic model of the crisis management from the perspective of an event can be described as follows [107]:

- ***Prevention:***

- is the dominant idea of crisis management
- responds to analyzed risks and uses the tools to minimise them,
- increases the level of security systems,
- creates a system of monitoring and evaluation of risk factors,
- reduces the likelihood of the emergence of crises,
- reduces the cost of removing the negative impact of the crisis.

- ***Crisis planning:***

- creates the conditions for the processing of detailed emergency plans to deal with the crisis,
- prepares to all foreseeable crisis events and the crisis management creates the conditions for the crisis at a given time and space,
- summarises the needs and requirements necessary for dealing with the crises and confronts them with the capabilities of an enterprise,
- determines the forces, means and resources needed to address the crisis.

- ***Responding to the crisis and its solution:***

- assumes the introduction of an effective system of warning and alert,
- has a character of a unique and ongoing process carried out on the basis of a qualified decision and without the problems,
- requires centralization and coordination of process management during the crisis to the nearest and most appropriate level,
- is carried out via the rescue, location and liquidation work,
- is characterized by personal responsibility, courage and determination of executive and managerial crisis management staff.

- ***Recovery:***

- aim of recovery is to return the company to the stable condition,
- majority of it is done in several stages,
- crisis management contributes only partially,
- allows returning to the conditions existing before the crisis.

The process approach to the crisis development in the company perceives the crisis as global and never-ending.

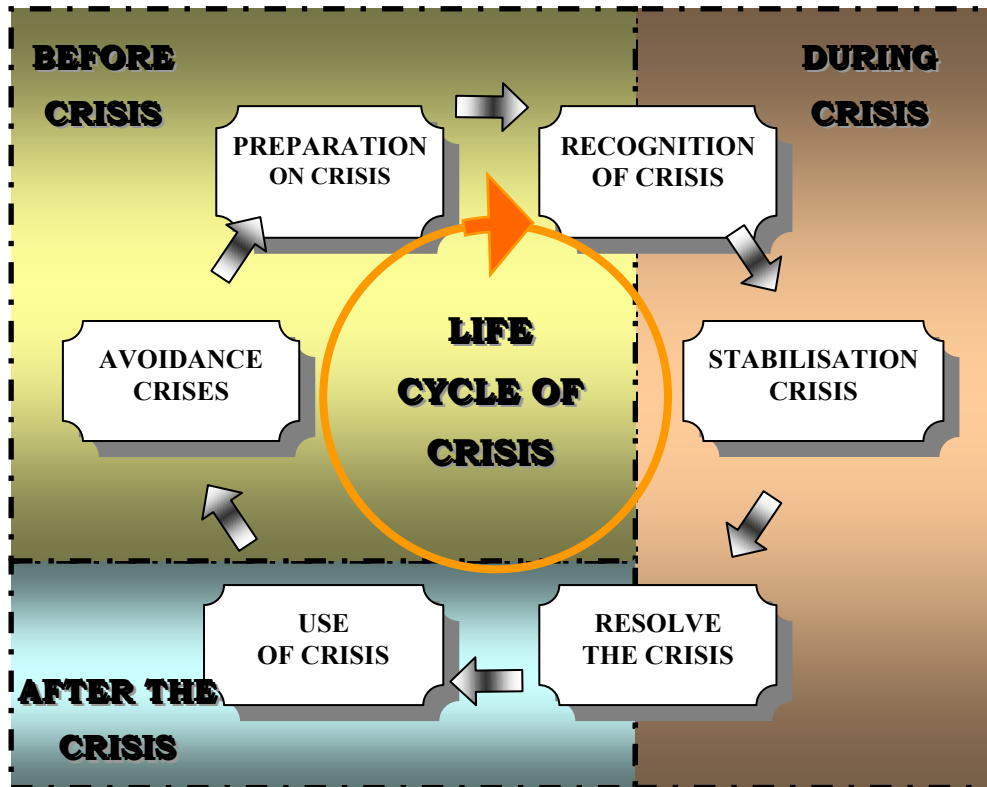


Fig. 3.4 Model of crisis management in its life cycle [68]

As already mentioned, every business goes through at a certain stage in its development of the crisis. If it can handle it, its existence goes on and the company further develops. The use of the conclusions of one crisis should help the company handle the next crisis in future. The utilization of the conclusions and insights of one crisis is the beginning of the next cycle of the new corporate crisis.

The life cycle of a business crisis is a continuous process (Figure 3.4) consisting of three stages and six phases:

**I. Stage before the crisis** consists of the following phases:

1. **Avoiding the crisis**, which is based on knowledge of the financial and economic situation of the company and its subsequent implementation of prevention. The analysis of the company is focused on the prognosis of the future status and trends.
2. **Preparing for the crisis**, which aims at identifying the hazards and risks and the company activities. The preparedness to a potential crisis is associated with the following advantages:
  - the company reduces the number of calamities and crises that need to be addressed,
  - enterprise life cycle is longer,
  - company achieves better financial results.

**II. The crisis** stage includes the following phases:

3. **Recognition of the crisis** from the normal fluctuation in the company's performance is a challenging process. Only the enterprise is considered healthy if there are no doubts about its future.
4. **Stabilization of the crisis** consists of the identification process, by which the company realizes that it is in crisis and the process that responds to the crisis and adapts to changes.
5. **Resoution of the crisis** occurs when by the diagnosis the state of crisis in the company is confirmed. The intensity of interventions and measures taken by the firm to address the crisis must reflect the seriousness of the problems in the company.

### **III. Phase of post-crisis phase consists of:**

6. **Use of the crisis** is a prerequisite for successful following problems and crisis situations in the company.

Different phases of corporate crisis, as seen in the crisis management process approach is discussed in Chapter 4.

### **3.5 Crisis management tasks in various stages of corporate crisis**

The crisis management should not be initiated but by the crisis itself. A comprehensive view of the crisis management in professionally controlled companies include the elements of prevention of crisis situations.

Mitroff, a leading world expert in crisis management, puts the emphasis on preventive measures designed to anticipate the crisis situations. Based on the premise that the crises are an inevitable and permanent attribute of modern society life, it is necessary to identify and evaluate the current warning signals, which are heralding the upcoming crisis. Consequently, it is possible to manage and deal with the crisis situation more efficiently. Powerful tools for managing the crisis situations are especially soft forms of control, such as the moral quality, corporate culture and unconventional ways of thinking.

Mitroff consistently distinguishes pre-crisis stage, as a precursor and the crisis stage, as a consequence, while for both stages defines the individual files of crisis management measures and recommendations, thus creating a normative model for the crisis management.

In various periods of the crisis management in the enterprise, the crisis management tasks differ. In principle, they can be divided into three groups according to the life stages of the crisis, the tasks to be carried out before the crisis, during the crisis and post-crisis business. The tasks are performed at different stages by the crisis management executives, whose work specifies in particularities, and which have to meet other requirements than the corporate managers.

The tasks of the crisis management are different in nature, scope and importance of the various levels of control and in the individual solutions to the crisis situation. The tasks of the crisis management are classified according to the period, when they carried out:

***A. Crisis management tasks before the crisis occurs:***

- processing and adoption of a comprehensive strategy of the crisis management in terms of the enterprise development,
- building of the crisis management system and its continuous adjustment in accordance with the changing external and internal conditions,
- adoption of the principles of the crisis management and continuous replenishment and adjustment,
- identification of potential crises and their anticipated negative effects,
- elaboration of disaster plans,
- preparation of the solution to the crisis, the processing of the methodological procedures and activity plans,
- elaboration of detailed plan connections (each system worker has to know to whom and in what cases call),
- continuous improvement and modernisation of technical equipment of the crisis management (creation of computer networks and databases) and its powerful features and the introduction of new technologies into practice,
- carrying out exercises and drills,
- organizing training and not only for workers, but also for all the crisis management which may affect the impact of the crisis,
- economical management with the material and technique of the crisis management in accordance with specified principles, as far as possible deal with the requirements for the rental of equipment and techniques for the normal operation,
- reducing the risks in response to the evaluation of the possibilities of developing crisis phenomena,
- training for smaller-scale emergencies, testing the system and technology modification of the system on the basis of experience,
- implementation of an effective control of the activities on their own level and subordinate components of the crisis management
- continuous monitoring of hazardous phenomena, assessment of their levels and adoption of measures (elimination of negative factors).

***B. Crisis management tasks during the crisis:***

- introduction of the crisis management system on the basis of the initial information about the crisis,
- obtain additional information on the crisis,
- correct and powerful elements to deal with the crisis after receiving the detailed information,
- determine the official spokesman during the crisis and the provision of information to the media from only one official site,
- interruption of all activities that are not related to the solution of the situation, and dedication of the rescue organisation, location and disposal work only,
- prevent the spread of panic, regular and sufficient information,
- adoption of preventive measures against the escalation of the crisis,
- declaration of extraordinary and special status in the enterprise mode, depending on the extent and nature of the crisis,

- statement of special economic measures (e.g. stopping the production that could negatively affect the course of the crisis and its level, on the other hand, the introduction of the production, which supports the process of winding-up the crisis),
- regular reporting the information on the management of the company during the crisis,
- restore normal mode after completion of the work related to the solution to the crisis.

***C. Crisis management tasks in the period after the crisis:***

- analyzing the course of resolving the crisis, evaluating the achieved level and propose further steps of the consequences until they reach the pre-crisis situation,
- assessment to what extent the prepared documentation meets the site personnel, material and technical equipment, as well as the actual conditions of the proposed technology solution to the crisis and propose any changes and modifications,
- ensure the technical solution, and refill store equipment and materials used by the crisis management for the solutions during the crisis,
- ensure more intensive and detailed monitoring of risk factors,
- resumption of routine activities.

#### 4 STRATEGIES DEPLOYED IN COMPANY CRISIS LIFE-CYCLE STAGES

Crisis development of the company, which is considered as a process, a life cycle that can be divided into three stages and six phases. If the crisis is perceived as pervasive and is a never ending process, it can be represented (Figure 4.1) as a closed cycle.

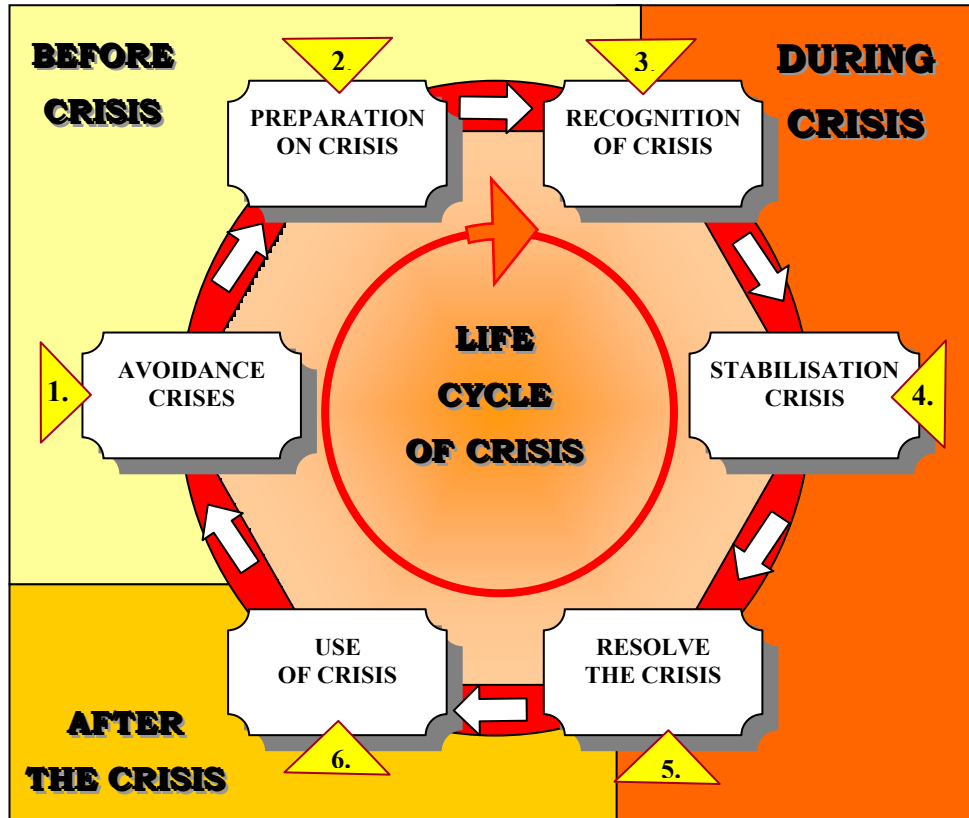


Fig. 4.1 Life cycle of a business crisis [69]

Various phases of corporate crisis passes are further elaborated in detail.

##### 4.1 Avoiding the crisis

The purpose of the company existence is to grow its market value, which is secured only if the business activity is efficient. Therefore, the crisis that reduces the efficiency of the enterprise, is not favorable for the company and the company tries to avoid it. The strategy of avoiding the crisis can be divided into:

- **Strategies elimination of the crisis outbreaks**, which seek to prevent the emergence of the phenomena, which could potentially jeopardize the enterprise. They refer to the activities taking place at a time when the firm is in the period of stagnation or growth. These are primarily:
  - **Strategies of abandoning the areas** that start to be less efficient and profitable and the parallel development of new products and services and customer satisfaction research starts.

- **Strategy of product innovation** and services, which are directly linked to new investments and research and development.
- **Strategies of investments to improve safety and security**, which are utilized due to the advantage of additional opportunities provided by the market, rationalization of production, purchase and modernization of the production base. The most frequent investments are focused on manufacturing, which forms the core of the enterprise.
- **Strategies to avert the crisis**, aimed at the early recognition of crisis development based on the analysis of indirect effects operating around the company and early deployment of countermeasures. To avert the crisis we use:
  - **Strategies of early detection of issues evolution** which represent a specific form of market research and marketing. An early warning system is based on a warning signals having various degrees of ability to predict the crisis:
    - *Comparison of plan and reality* working with historical data, therefore, this procedure can predict the future and highlight the potential risks. When moving away from the planned values, the company is forced to take countermeasures.
    - *Delayed signals* are indicators based on direct relation to the development in the market and around the company. The delayed signals do not generate a sufficient time span before a crisis occurs to respond adequately to the impending crisis.
    - *Weak signals* are recognizable much earlier than the delayed signals. The weak signals appear most frequently in the overall economy and the socio-political sphere, while having an indirect and long-term impact on the business activity.
  - **Strategies defending the escalations**, the essence of which is the activity directed to prevent the crisis. Time factor is crucial with these strategies.

For the development of the mentioned strategies to avoid the corporate crises it is necessary to recognize the financial and economic situation in the company, and only then it is possible to carry out the prevention. In ascertaining the status of the organization it is particularly important to predict the future state of the company and determine its future direction.

#### **4.1.1 Prevention of crisis in the enterprise**

The business management has the opportunity to fundamentally affect the business risk and shall recognize potential risks and know the methods and identify the possible ways to reduce the risk in the implementation of the business plan. Each enterprise has to decide which risks are to be retained, which reduced, and which to avoid.



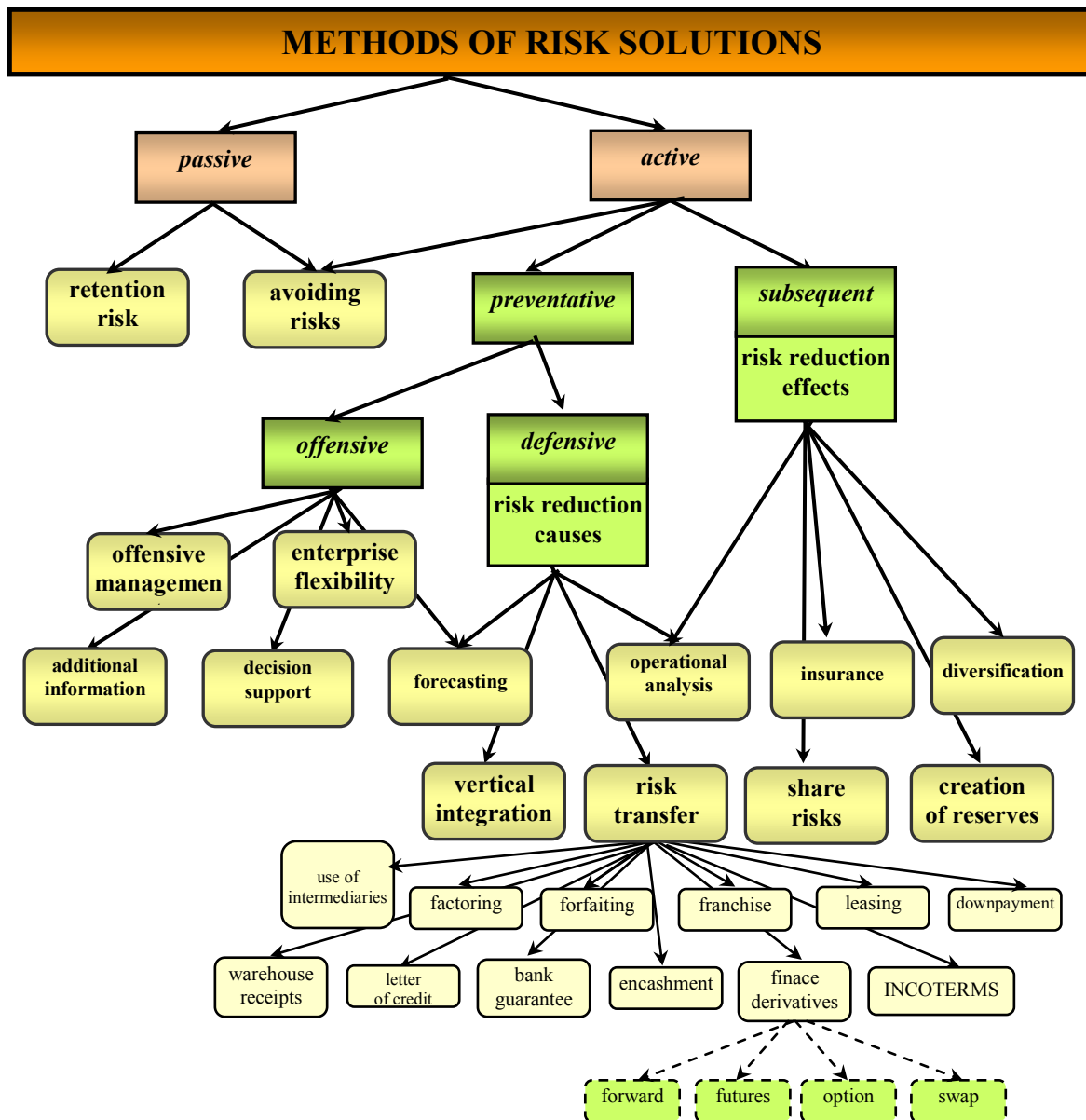


Fig. 4.2 Classification of methods to address risks [107]

Basic methods of risk reduction methods are shown in Figure 4.2, which are arranged according to their areas of influence and practices aimed at reducing the causes and consequences of risks.

#### 4.1.2 Prognosis

The increasing complexity of the business environment raises along with changing customer needs need to know how they will develop key variables on which the strategy development and business efficiency depend. A lot of management problems arise because of ignorance or lack of knowledge of the future situation or of the degree of its uncertainty. Therefore, currently, the managers begin to pay close attention to methods allowing the future values prediction of key variables that influence their decisions. Economic variables often show trends that are predictable. Knowledge and quantification of development trends allow the managers reliably and efficiently make decisions. The need for forecasting has therefore its logical reasoning.

Forecasting methods in business processes are irreplaceable. They belong to the class of deterministic methods that may be used to reduce the risk of decision-making problems at the operational or tactical level of management. Reducing the risk on a reasonable level means to anticipate, predict, and prepare variables of possible development scenarios of the company and its characteristics.

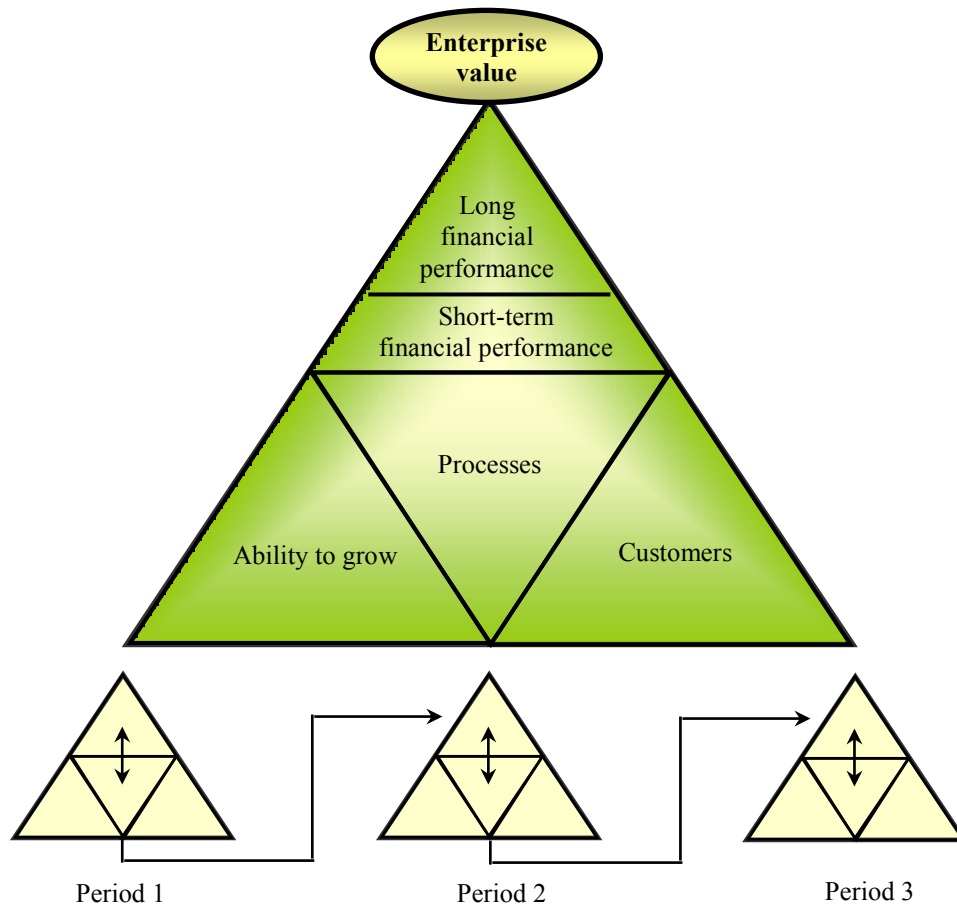
In relation to the prognosis of the company development it is crucial:

- **Respect the causality:** Everything has its cause that has triggered the condition. Every action causes a reaction, creating thus a complex map of causes and consequences.
- **Nonlinearity of relations:** For each reaction, it is necessary to estimate its character.
- **Delay of response in time:** In the business activity not all decisions appear immediately. Some of them have a longer time effect or cause changes over the time, which is to be estimated.
- **Time dimension:** Decisions need to be assessed from the point of short and long-term views, because their impact may vary.
- **Company integrity:** Not all decisions are taken in the company, or are advantageous for the enterprise as a whole. Some decisions are beneficial only for certain business units. In decision-making the result of a decision from the perspective of the enterprise should be considered.
- **Bottleneck:** From the point of the growth of efficiency and business performance it is necessary to address the bottlenecks in the enterprise. All other decisions which are not connected with the solution of bottlenecks do not determine the overall efficiency and performance of the enterprise.

Future situation, which the company wants to achieve, can be represented by means of causal maps. For its preparation, it is necessary to map the layout and the company's potential for future financial performance and efficiency.

The prognosis of the future is based on the current state of the business, which can be described via the financial situation. A map showing the current position of the enterprise is made, revealing thus the biggest issues and identifying the priorities on which the business should focus its attention. The map proceeds from the present to the future, creating thus an implementation plan. The enforcement and implementation of the selected strategy of the enterprise is associated with the resistance to the changes needed. The greatest benefit of the strategic maps is represented by their ability to illustrate the whole corporate strategy's.

The current financial situation is the result of all past and current decisions, which affect the present and future. In the strategy development and implementation it is necessary to respect not only the interdependence of different perspectives, but also the relationships at the time, and links to the surroundings, as well as to the internal relations.



**Fig. 4.3** Development of values in the company

The growth of company market value is the ultimate goal of all its efforts. The prerequisite for the radical increase in the market value of the enterprise is represented by the discontinuity in its performance and its radical increase, therefore, it is necessary to identify the drives of radical increases in performance. For the enterprise, its long-term financial performance and efficiency are crucial.

The strategic map shows selected indicators, planned values of these indicators in the form of objectives and the drives able to affect of values for each base company prospect. It clearly defines the roles and responsibilities for their execution. The proper selection of indicators linked to the remuneration system is important. The indicator must determine the drive action.

The basis for making the strategic map is represented by finding where the company creates its value. It is necessary to identify the location and cause of the values. By sharing the indicators affecting the strategy the indicators can be divided according to Porter's value chain. A general overview of areas, which contribute to the creation of values is shown in Figure 3.4. The activities of the company can be divided into primary and support ones.

The strategy map is a tool that provides the employees with a clear idea about the direction of their further work in order to achieve the business goals. It allows them to coordinate the work and direct it to the desired objective enterprise. The map is a visual idea of the critical points and their critical enterprise relationships affecting the company performance and efficiency.

The components of the strategic map are as follows:

- strategic objectives for four basic perspectives,
- strategic output indicators for all strategic objectives,
- strategic drives of output indicators,
- balance of strategic output indicators and drives via diagnostic indicators monitoring the means of achieving the strategic indicators,
- chains of causal links:
  - links of corporate objectives,
  - links of indicators
  - links of indicators and their drives.

The strategic map **shows**:

- targets for sales growth,
- target markets of customers with the growth in profitability,
- value for customers leading to an increase of the purchase volume or sales of higher margin,
- key role of innovations and excellence of products, services and processes,
- investments needed for people and systems to create and sustain the planned growth.

To understand the creation of the company value in the information age, the system of balanced indicators is used, which can quickly summarize:

- required knowledge and skills of employees,
- existing and necessary strategic capacity and business efficiency,
- value of goods supplied to customers,
- increasing value for business owners.

The strategic map is developed from the present to the future, creating thus an implementation plan. The basis for the preparation of the strategic map is represented by knowledge of current financial situation. The important thing is to know the causes and variables which affect the financial results. They record all key factors which determine the value of the enterprise as well as the priorities identify, to which the enterprise should focus its attention. Various aspects affecting the company efficiency and performance is most commonly divided into four perspectives, according to Kaplan and Norton's Balanced Scorecard.

The future position of the company, which the company wants to achieve is the output of the strategic map. For its preparation, it is necessary to map the layout and the company's potential for future financial performance and business efficiency. Enforcement and implementation of the chosen strategy in the enterprise is associated with the resistance to necessary changes induced.

The strategic map expresses the way the company wants to transform various business resources onto desired outcomes. To create your own strategic map, based on the Balanced Scorecard, you can use the sample map shown in Figure 4.4.

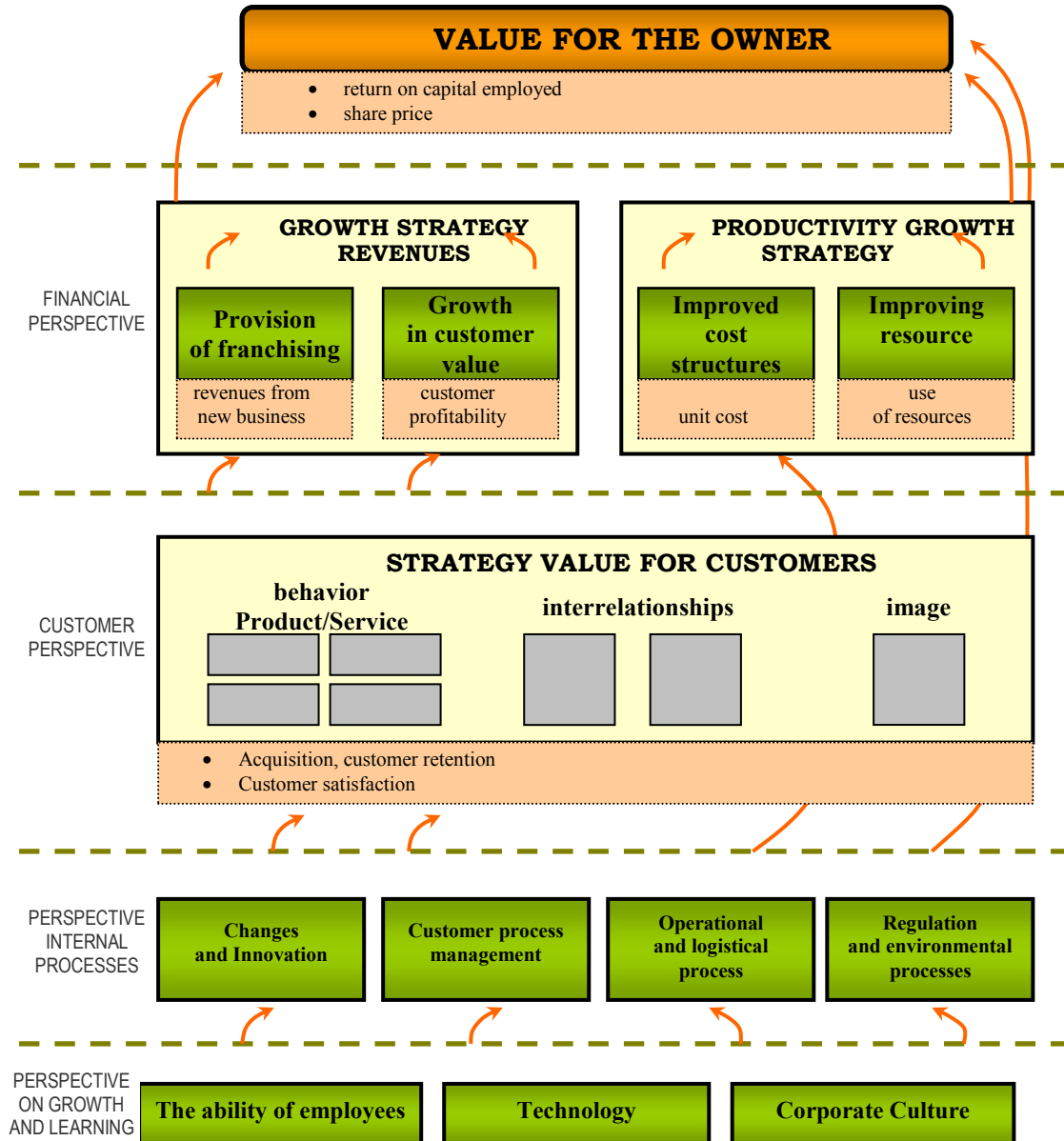


Fig. 4.4 General strategic map of Balanced Scorecard [171]

After modification the sample strategic map can be applied to various sectors of the national economy, industry, insurance companies, banks, businesses and trading services, medical facilities, government institutions, non-profit organizations and the like. The executives can adapt the model to develop a suitable strategic map that will reflect their business relationships.

The best way of making the strategic map is represented by proceeding from top to bottom. It starts with drawing the "destination station" and describing the ways and means leading to their achievement.

As a first step, the managers have to re-evaluate the corporate vision and values the enterprise is built on, and in which it believes. Based on this information, the managers can develop a strategic vision and determine what the company wants to achieve. The enterprise vision draws a clear picture of main corporate objectives, for example, to become a leader in

making profits in a particular industry. The strategy should define the process as a determined vision of the enterprise strives to reach.

- I.* After defining the company vision and strategy, the creation of a **financial strategy** to grow the company's value follows. Businesses may decide for one of two basic financial strategies:
- **Sales growth strategy**, which consists of two parts:
    - **Franchising strategy**, which is aimed at achieving revenues associated with the growth of the market share, which is achieved by creating new products, new markets and new customers.
    - **Value growth strategy for customers** aimed at achieving the sales of existing products, sales and customers. The strategy is aimed at creating good relationships with customers and increasing their confidence and loyalty to the company.
  - **Strategy of productivity**, which also consists of two parts:
    - **Strategy of improving the company cost structure** by reducing direct and overhead costs.
    - **Strategy of efficient use of resources** in the form of reduction of current and non-current assets.

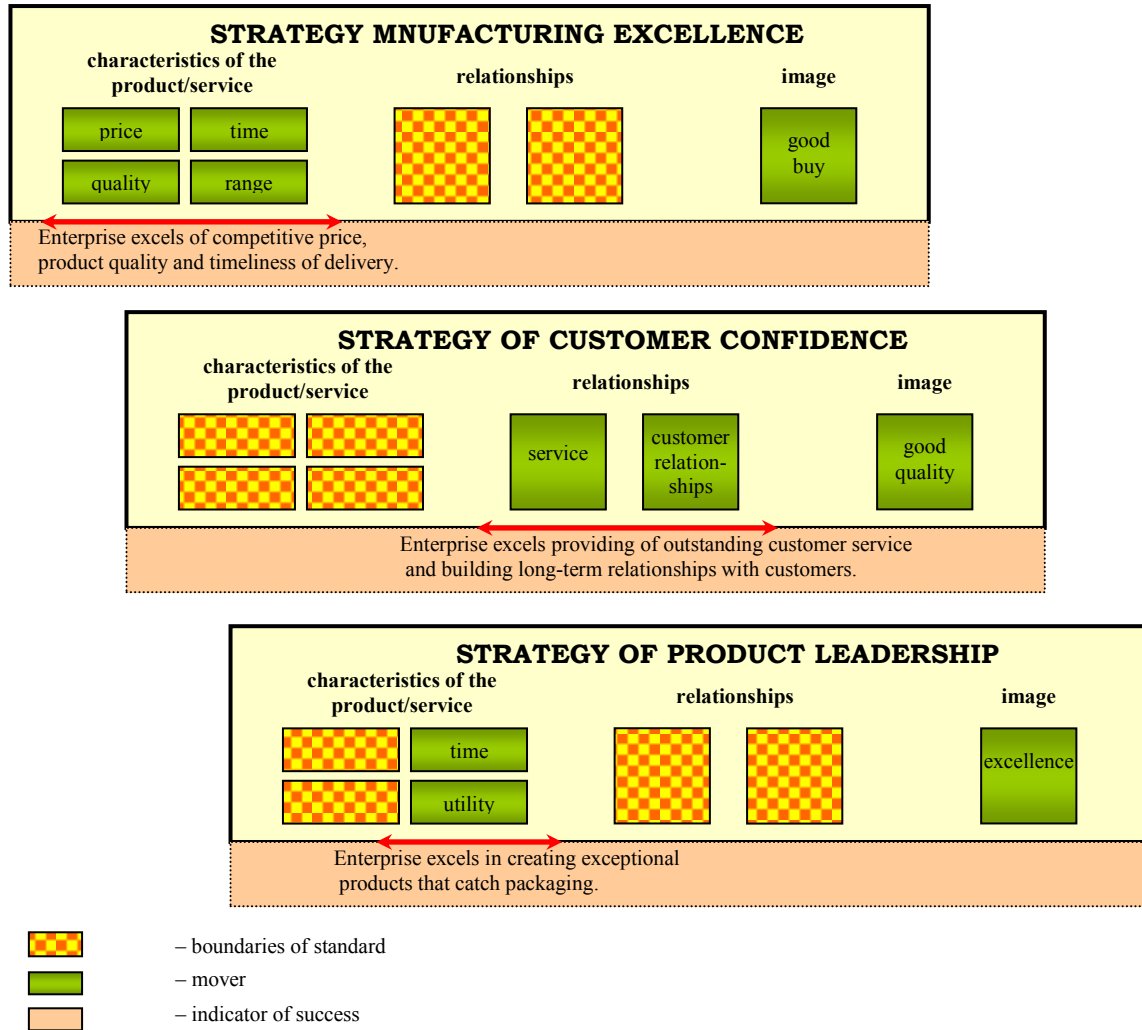
In general, the productivity strategy achieves the desired results in a shorter time period than the growth strategy. Nevertheless, the main benefit in that the strategic map looks for the opportunities to improve the company's financial performance via the revenue growth and not by reducing the costs and more efficient use of resources. The balanced use of all financial strategies contributes to the growth of the company's value.

- II.* The core of any business strategy is represented by the **strategy of creating the value for customers**, which represents the sum of:
- nature of products and services,
  - relationships with customers,
  - corporate image.

The mentioned aspects of customer strategy defines the way of distinguishing the company from its competitors as well as the business relationships with target customers. Businesses try to excel in one of three areas, while the other two areas are maintained within the standard limits.

Regarding the customer perspective, most businesses mainly decide for one of following three strategies:

- **Strategy of manufacturing excellence,**
- **Strategy of customers' confidence,**
- **Strategy of product leadership.**



**Fig. 4.5** Variable strategies of value creation for customers [171]

The enterprises that promote the production strategy of excellence, offer the products and services such as price, quality and range comparable to competing products or services. The offered products are delivered on time and immediately after ordering.

In implementing the strategy of building the confidence with customers, the companies emphasize the quality of their relationships with customers, providing warranty services and solutions to any problems of customers.

The businesses that choose to apply the strategy of product leadership have to focus on functionality, features, overall performance and effectiveness of the products sold and services provided.

If an enterprise has an image of customer and financial perspective built, it can proceed to the definition of how the value for customers and productivity increase for achieving the ultimate goals of the company can be designed.

**III. Perspective of internal processes** and records the critical activities of an activity, which can be divided into four levels of processes:

- increasing the sales via changes and innovations of products and services, penetration into new markets and new consumer segments,

- increasing the customer value by deepening the relationships with existing customers,
- achieving the manufacturing excellence by improving the management of supplier-customer relations, cost management, quality and progress of internal processes, resources and production capacity,
- developing a good position of the company in relation to its surroundings and external interests.

Most businesses that adopt the strategy oriented on changes and innovations, or the growth of added value for customers evaluate only the level of costs and quality of their activities and forget to evaluate the changes and customer processes.

These companies do not have indicators for evaluating objectives to be achieved developed, thereby cause the problems in implementing the growth strategy.

Financial benefits of improving the business processes manifest themselves gradually in several stages. Cost savings associated with an increase of production efficiency and process improvement are reflected in the short term. The sales growth as a result of improved relationships with customers is reflected in the medium term. The growth of innovations and changes brings sales and increase profits in the long term period.

**IV.** Every strategic map is based on the **perspective of learning and development**, which characterizes the core competencies and skills, technology and corporate culture. In order to achieve the targets the management directs the human resources and technology in the enterprise. Despite the fact that the managers are aware of the importance of such a perspective, generally, they have difficulties to define adequate and appropriate targets [171].

#### **4.1.3 Use of synergy as a tool to prevent the business crisis occurrence**

The synergistic effect can be used as a means to prevent the corporate crises. It can be assumed that in the business environment of the third millennium, a synergistic effect becomes a critical business objective. It is a criterion by which it is possible to assess the competitive potential and competitiveness of enterprises.

**Synergy** expresses a phenomenon whose essence is seemingly and mainly mathematically illogical result reflecting the fact that the *whole may be greater than the sum of its individual parts* [110]. The synergistic effect is the effect of the whole which is different from the sum of effects of individual parts of the whole. The synergistic effect can have three basic forms:

- **Positive synergistic effect** occurs when the effect of a whole is greater than the sum of effects of individual parts of the whole,
- **Negative synergistic effect** occurs when the effect of the whole is less than the sum of effects of individual parts of the whole,
- **Sterile synergistic effect** occurs when the effect of the whole is equal to the sum of the effects of individual parts of the whole.

From the dynamic point of view there are two types of synergistic effects:

- **integration effect** generated by composing the individual parts into a whole,



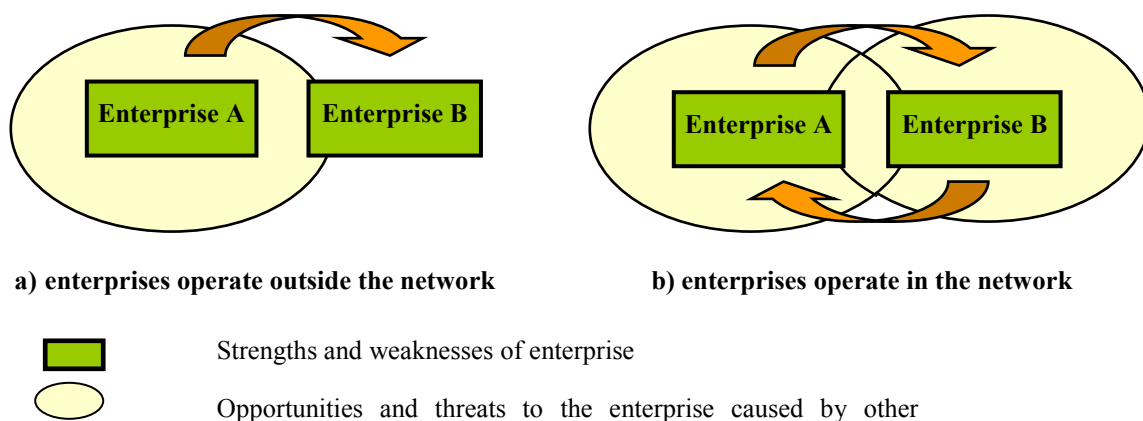
- **disintegration effect** arising from the effect of a decomposition.

The force field has properties of cobwebs and is represented by a network. The strength of bonds if the force field is a bundle of nodes. Joined nodes manifest as a centrifugal or gravity forces. The potential has its position in the force field, which affects the efficiency and flexibility of forces. From the point of signs the elemental, individual potentials cannot be divided into to other characteristics. It can be divided only in terms of its use, which is expressed by its practicality and usefulness. The complex potential can be divided into sub-potentials.

The synergistic potential force field is a combination of size and usefulness manifestations of individual potentials, strength of their relations, interrelations and their positions in the force field. The individual potential in the force field is increased or decreased with respect to the strength of other potentials in the force field, the size of attractive forces oriented on on the potential of the force field, the size of the centrifugals force directed towards the potential into the force field and its position in the force field.

Despite the attractive forces are large enough, the new bonds of potentials may not be reinforced. It is due to the existence of contradictory potential in the form of resistance to new bonds, or to strengthening the existing bonds. If the enterprises work independently, most often it comes only to a one way action (Figure 4.6 a), where the stronger enterprise influences and determines the activities and behavior of the weaker one.

The network of enterprises is understood as a group of businesses that use common resources to work together on joint projects. In the network there is a mutual influencing of the the companies participating in the network, as shown in Figure 4.6 b. The purpose of the enterprise networks is to achieve the synergistic effect. In practice, the networking of companies not only positive synergistic effects, but also negative, or zero synergy can occur.



**Fig. 4.6** The synergistic effect of the network in dependence on the interaction of enterprises [31]

Synergistic business must be based on value-creating networks that create the value for customers, but also for the businesses themselves. The enterprise in the synergistically working network is at simultaneously its producer, but to large extent also its consumer. This leads to strengthening the feedback potential of the enterprise in the network.

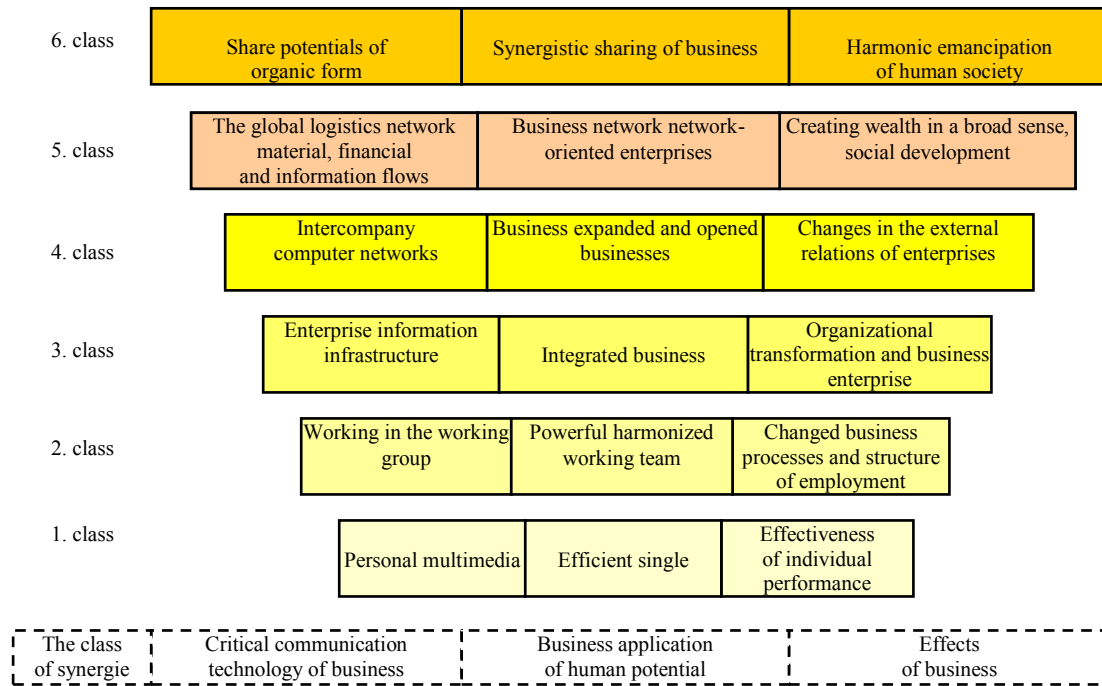
The synergistic effect requires a qualitative change in human relationships. It works with the psychological element, such as motivation. The synergy is based on three important principles and relations among people:

- **friendliness,**
- **cooperation,**
- **cohesion.**

The most effective way to induce these elements of mutual relations resulting in the synergistic effect is represented by the understandable and attractive formulation of the main goals of the enterprise, which make each individual believe that his/her personal goals can be achieved and only if they align with the objectives of the enterprise. The main goals of the business simply become each employee's personal goals on all organizational levels. The employees are then willing to work beyond their obligations and create an environment where friendliness, cooperation and cohesion magnify the result effect.

Effective synergistic relationships cannot be imposed or enforced by the organization. The synergy does not stem from the formal fulfillment of obligations, but from a sincere and conscious identification with the main corporate objectives. Flexible, responsive and resilient enterprise is not built on the basis of its internal policies, but on the basis of cohesion, cooperation and friendliness of all the executives. Therefore, all managers should participate in defining the main corporate objective. Consequently, the managers have to identify with the main objective of the company internally as well.

The basis of the process of building the synergistic effect is to share information, data and knowledge. Interconnectedness of human potential to the development of communication technology and the development of synergies in business, with a view to changing developments in society, is shown in Figure 7.4.



**Fig. 4.7** The role of the human potential for synergistic effects [110]

Synergistic business in terms of new economicsy can be characterized by five dimensions building dynamically a changing pyramid of synergistic business:

- content,
- form,
- space,
- communication,
- time.

Four basic dimensions of the pyramid are shown in Figure 8.4. Each dimension has three layers or levels. Small and medium enterprises are mostly on the lowest levels of the pyramid. Larger enterprises apply principles void in higher levels of the pyramid. Top positions in the pyramid are achieved by particular transnational corporations, mostly in relation to communication assumptions.

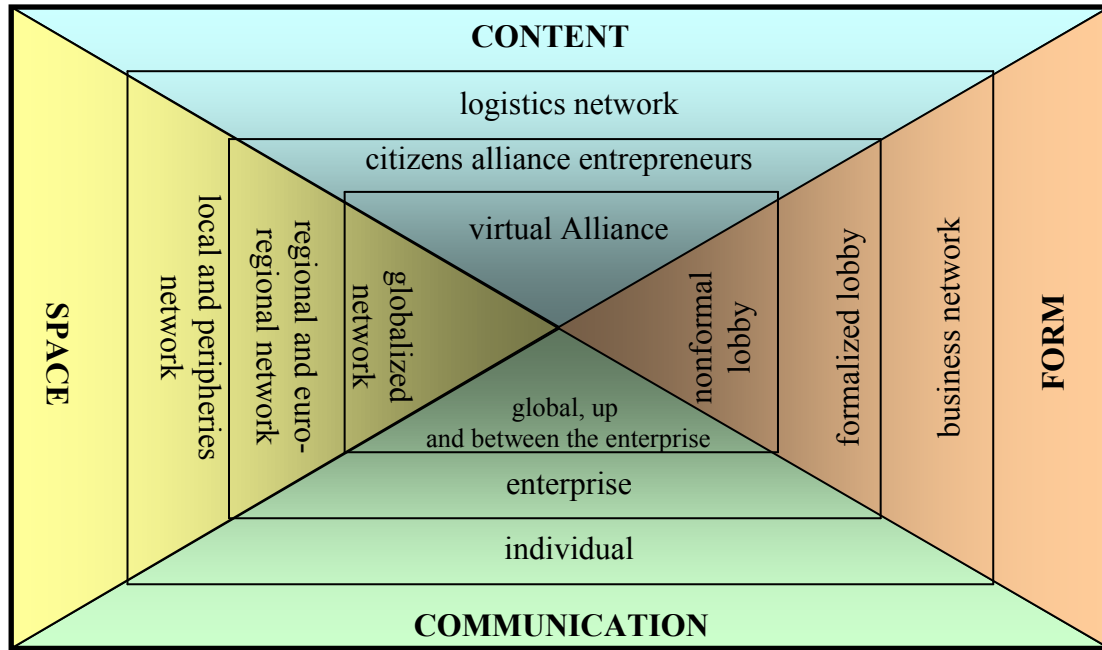


Fig. 4.8 Fundamental dimensions of synergistic business pyramid [110]

The fifth dimension – the time, should be seen as the dimension of constant change. The pyramid is characterized by dual-type changes:

- **Pyramid constantly shifts** in width and height. It is caused by the destruction of old branches of the undertaking and substituting or supplementing it with new activities.
- **Pyramid dynamically moves and changes** according to the form of business and in dependence on entities involved in the synergistic effects and conditions of human society and business development.

#### 4.1.4 Impact of corporate image on the origin and development of corporate crisis

The success of managing the crisis is affected by the image of the company before the crisis. In practice, it is proved that the dampening effect of the reputation of the company and its products is the greater the more prominent the actions are associated with building the positive image of the company. The classic activities contributing to the formation of good business reputation comprise: day of open house, provision of above-average social conditions for company employees, sponsoring cultural and sports events and the like.

The building of the positive company image must be thought about before the crisis, because most of the activities during the crisis are inefficient and lead to unnecessarily expended funds.

The impression that remains in the customers in contact with the company staff contributes significantly to shaping their view on the entire enterprise. This impression is formed only marketing and sales staff, but by all workers who come in contact with the customer for other reasons once or regularly as well. Therefore, all employees coming in contact with customers should be trained to communicate with them.

Sales differs from other company operations in that it takes place in the environment of permanent insecurity. Therefore, the selection of sales personnel must take this into account.

The vendor must be such a person who is able to cope with uncertainty and can use it to their advantage better than competition sales staff.

Fundamental characteristics and skills of sales professionals are as follows:

- **Initiative** expressing self-determination, not waiting for the tasks, conflict situations at their discretion and use of time, so that it is utilized for achieving the sales goals.
- **Custom judgment** that requires abstract thinking, designed to achieve the target of the business meeting and the needs and wants of customers.
- **Sense of trade** enabling the trader to assess the readiness of the customer to buy the product.
- **Commodity knowledge** presents a detailed knowledge of the parameters of the products that the company offers as well as of the products offered by the competitors. They must know their advantages and disadvantages for the customer. The expertise of the trader should arouse the feeling of confidence in the customer.
- **Communication** allowing the trader to formulate ideas, to adapt the communication form and level to the customer.
- **Presentation** which has to be adequate and polite, even in cases where the business does not succeed.

## **4.2 Preparing for a crisis**

Enterprises, depending on the readiness to the crisis can be divided into:

- **proactive companies** that are prepared to the crisis,
- **reactive enterprises** that are susceptible to crises.

The company readiness to the crisis does not require to be prepared for each conceivable danger, but there are ways to prepare strategies for reducing its own vulnerability. The proactive businesses recognize three basic forms of a risk:

- **Natural calamities and disasters** for which the risk management is used.
- **Normal accidents** associated with the failure of the technology. Preparation to this type of the crisis management is complex and it involved the project planners, managers and others responsible staff.
- **Deliberately caused accidents**, i.e. abnormal incidents, which include e.g. terrorism, in particular.

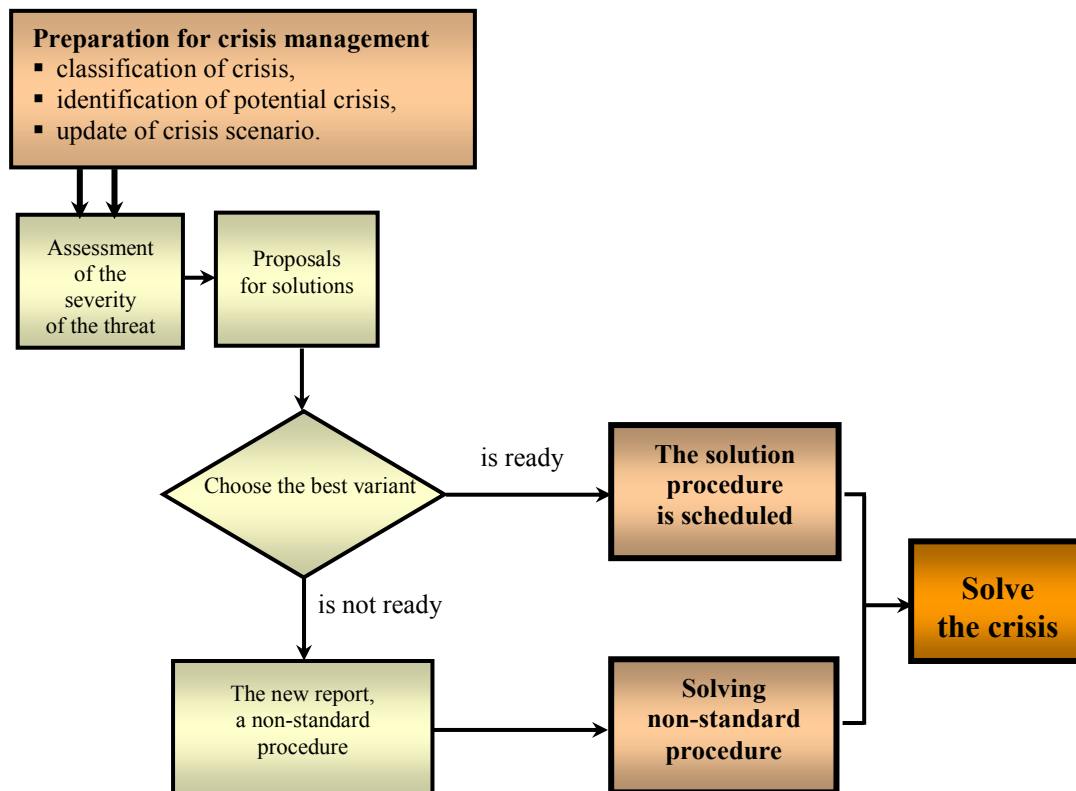
The readiness of the company to a potential crisis is associated with the following advantages:

- company reduces the number of calamities and crises that need to be addressed,
- enterprise life cycle is longer,
- company achieves better financial results.

The proactive enterprises build crisis centres, which have the following three obligations:

- **Plan the corporate portfolio**, which consists of at least one crisis resolution options for each group dealing with the prevention and emergency planning response to the accident.
- **Pay attention to the signals** that necessarily preceeded the crisis and **draw attention to the impending threat** of the responsible executive.
- Carry out audits, training and install mechanisms to prevent the crisis.

For crisis management new activities are necessary, i.e. the prevention of crises and the tools for mastering the crisis. Most business strategies formulate low efficient measures, since they reflect only predictable events. The art of the crisis management, however, lies in mastering not only the foreseeable but also the unforeseeable events, it is therefore necessary to create crisis scenarios. The process of creating the crisis scenario is shown in Figure 4.9.



**Fig. 4.9** The process of developing a crisis scenario [107]

An enterprise should be prepared for the emergence of a crisis situation, which may result due to the variety of internal and external causes. At the time of preparation for the crisis it is necessary to:

### ***1. Assemble a team of crisis managers***

The team of crisis managers should consist of specialists from the various functional areas of the company, who take over the tasks related to the prevention of crises, as a part of their employment duties in the company. The member of the crisis management should possess the following competencies:

- **ability to understand the tasks**, for which critical thinking and strategic foresight are necessary,
- **ability to perform tasks and provide activities and processes** requiring an active approach, self-confidence, self-control and flexibility,
- **ability to lead teams** via motivation, interpersonal skills and interest in business outcomes.

Crisis management team should consist of the following members:

- member of management,
- worker in the field of production,
- administration worker,
- sales engineer,
- worker is responsible for the enterprise safety,
- member of operation board.

The importance of the using the specialized counselor, who is not directly from the company, but can perceive it from the outside without prejudice to the company burdens and has the ability to bring new thoughts and ideas.

## ***2. Training of the crisis managers team and determination of the time course***

The crisis manager must be able to detect the outbreak of the crisis quickly, which may be represented by various weaknesses of the enterprise and the flexibly propose the variables of its elimination. For this reason, the preparation of managers to crisis situations includes:

- training of skills to perceive the crisis signals,
- rehearsal procedure (performance of duties) in the course of the crisis,
- training of communication with the representatives of the public affected by the corporate crisis.

**The crisis schedule should be as follows:**

- within 2 months: develop the concept on the future company position on the market,
- within 6 months: first specific results,
- within 12 months: fundamental improvements that occurring in the predefined criteria,
- within 15 months: achieve significant turn of the company,
- up to 2–3 years: fundamental improvement of the company position, at least 80 % of indicators must reflect the crisis solution.

***In general, to overcome the negative economic trends in the enterprise two years are required.***

### 3. Determination of the enterprise crisis potential

The most important stage of the risk management process is represented by the identification of the enterprise management objectives. The task is to identify the significant risks or risk areas affecting the achievement of the corporate strategy.

For the purpose of proper and timely identification of risks, it is necessary to build a quality system ensuring a constant flow of information on the changing external and internal environment of the enterprise. An important role can be played by the internal audit and controlling. In most of the businesses the manager, who is responsible for ensuring the fulfillment of the necessary information, he has to monitor closely and precisely describe the relationship between cause and effect, in particular, in the following terms:

- cause of risk emergence – analysis of changes in market parameters,
- object of the analysis on which the discussed risks act – the enterprise and its activities,
- analyzed effects leading to the change of the property value, or company yields.

As a result of the findings and identification of risks there is a **list of possible sources of risks** and their possible connections. The identification of risks, in general, is based on the objectives defined by the senior management of the enterprise. After compiling the list of potential sources of risk scenarios of crisis situations, the catalogue of crisis situations scenarios is drawn up comprising a detailed description of crisis situations which may arise. The next task is to predict the emergence of these situations and determine the frequency of the occurrence or the likelihood of these situations.

In practice, it may not always be easy to subject each of these scenarios of detailed quantitative analysis of frequency and consequences when identifying the risks of a system, facility or activity and a large number of crisis scenarios can be got. In such situations it may be reasonable to arrange the accident scenarios contained in the catalog of crises, qualitatively and place them in a risk matrix denoting the various levels of risk, thereby producing the risks portfolio representing the homogeneous risk groups. The division takes place on the basis of two parameters (Figure 4.10):

- **probability** of risks occurrence,
- **severity** of the risks impact on an enterprise.

Subsequently, their relationships are examined and possible influences on various financial and non-financial variables.

		probability of occurrence of risks	
		low	high
the severity of the impact of risks on an enterprise	big	consider immediate action and have available a reserve plan	consider immediate action
	small	regularly monitor	consider measures

**Fig. 4.10** The matrix of the distribution of risks into portfolios

The matrix selection, which is the most suitable to the analysis given depends on the particular application (Figure 4.11). However, it is appropriate to record all the matrices



together with the estimated positions of all considered scenarios. The risk rate of the the assessed crisis situation scenario is given by its position in the matrix defining the extent of the risk. The most unfavorable position of R1, 1 on the other hand, the position of R8, 8 will be the most favorable regarding the severity and likelihood of risks. It is not meaningful to address the positions that occupy the top right and bottom left corner in this matrix, because the crises situations leading to the apocalyptic, catastrophic, or huge consequences do not threaten mankind so far. It also does not make sense to deal with the crisis whose frequency of occurrence is very low and the consequences are not great. However, the evaluator has to determine the boundaries of a particular matrix by himself.

The consequences of the crisis Multiplicity occurrence		nr	apocalyptic	catastrophic	huge	large	severe	serious	small	trivial	Truthfulness strategy	Probability value
			1	2	3	4	5	6	7	8		
Verbal	numeric	nr	1	2	3	4	5	6	7	8		
Very frequent	> 1	1	R <sub>1,1</sub>	R <sub>1,2</sub>	R <sub>1,3</sub>	R <sub>1,4</sub>						
Frequent	(10 <sup>-1</sup> , 1)	2	R <sub>2,1</sub>	R <sub>2,2</sub>	R <sub>2,3</sub>							
Usual	(5*10 <sup>-2</sup> , 10 <sup>-1</sup> )	3	R <sub>3,1</sub>	R <sub>3,2</sub>								
Occasional	(10 <sup>-2</sup> , 5*10 <sup>-2</sup> )	4	R <sub>4,1</sub>									
Rare	(5*10 <sup>-3</sup> , 10 <sup>-2</sup> )	5										
Unusual	(10 <sup>-3</sup> , 5*10 <sup>-3</sup> )	6								R <sub>6,8</sub>		
Almost impossible	(10 <sup>-4</sup> , 10 <sup>-3</sup> )	7							R <sub>7,7</sub>	R <sub>7,8</sub>		
Impossible	< 10 <sup>-6</sup>	8						R <sub>8,6</sub>	R <sub>8,7</sub>	R <sub>8,8</sub>		

**Fig. 4.11** Matrix defining the extent of the risk of the crisis situation scenario [107]

The result of the risk analysis must be represented by the documentation which clearly defines the various types of risks, information on their development and administration as required by the senior management. To each risk, or group of risks a specific person responsible for their management, including appropriate competence and adequate resources should be allotted.

#### **4. Development of crisis strategy proposals**

The distinctive feature and the key moment of the demanding process of enterprise reconstruction is represented by the moment of its inception. It is important to recognize the company status of the recovery processes at the time. At the moment of the beginning of an extensive and comprehensive recovery process the sophisticated and announced in advance termination of business activities occurs. Immediately after, in the form of an immediate turn the beginning of the extensive changes start, which means the emergence of a new business.

Depending on the stage of the business life cycle, in which the enterprise at the time of its recovery is, it is possible to examine the restructuring strategy, which are described in detail in a separate Chapter 7.2.2. The strategies are aimed at increasing the efficiency of the company, or to rescue the company from extinction. Considerations in the company

development stage, which is critical to the most appropriate from the point of corporate restructuring, particularly in terms of restructuring efficiency and the period when the restructuring is a necessity for the existence of the company, are also important.

### ***5. Detailed processing of crisis program, including the measures and tasks division***

Crises plans drawn up only to be hidden in the drawer, represent the planned measures for the case of a crisis situation emergence. The planned measures can be divided into three groups according to their nature:

- **Information measures**, which contain the lists of all persons to be informed at the earliest in case of crisis.
- **Measures to ensure against losses**, which are aimed at compliance with the following and carrying out the regular check-ups and safety measures and conduct of safety training for workers.
- **Measures to cope with the crisis**, which are drawn up for the different types of crises, depending on their extent. The measures also depend on the degree of the threat to the enterprise.

### ***6. Regular monitoring of implementation progress and strategy update***

Regular monitoring of the implementation progress of the treating process in the company and update of the business strategy should take place every three months.

## **4.3 Recognizing the crisis**

The views of the difference between the well functioning of enterprise and enterprise having troubles are varied. The main cause is represented by that the fact that the subjects which are carry out the evaluation are assigned different evaluation criteria used in measuring the weight. When assessing the company health, particularly the following criteria are used, some of which are complementary and some of them are contradictory:

- short-term yield,
- level of technology,
- qualifications of employees,
- economic benefits of enterprise,
- cost of research and development,
- concentration or diversification,
- dependence on market,
- long-term planning.

Healthy and well-functioning enterprise has the following characteristics:

- Has the financial return that sufficiently capitalizes own capital.
- Is able to meet the needs of customers, shareholders, creditors, employees, suppliers and the environment in which s/he operates.
- Has stable circle of satisfied customers.
- Its products and services meet the requirements of the market price and quality.

- Is continually dedicated to the market research and uses research findings to introduce new products and services to the market according to the identified customers' requirements.
- Has qualified staff who are constantly educated and properly motivated.
- Has optimal capital structure.
- Works with powerful and reliable suppliers of raw materials, semi-finished products and services.
- Has strategic location.
- Applies gentle approach to the environment.

Healthy business is such a business in which there are no doubts about its future. It is able to finance its activities, and generate sufficient profit to meet its obligations, which is used to invest in the company and, finally, ensures the adequate capitalisation of shareholders' investments.

The company, which is not able to meet the criteria, should take appropriate action to restore its vitality. The company may indicate its demise or threat of demise. All other circumstances that have an impact on business performance and create negative indications, can result in periodical variations in a performance of the company.

It is difficult to recognize when it is just about the periodic fluctuations in the company performance, and when the company actually gets into a crisis. For the assessment of the health of the company, it is possible to come out from the following Figure 4.12, which describes the business status from various aspects.

The financial value of the enterprise	A			B	C	D			E
	Solid enterprise			Venture enterprise	Difficult burden enterprise	Credit unworthy enterprise			Insolvent enterprise
Status	Threshold adjustment		Threshold risk	Threshold crisis		Threshold truth	Decline		Reporting insolvency
	⬇		⬇	⬇		⬇	⬇		⬇
Period	1	2	3	4	5	6	7	8	9
Activity	Healthy growth	Healthy stagnation	Adaptability own strength	Degree of risk	Critical stage	Suspicious handling	Grade idle	Redevelopment handedly	Judicial insolvency
Status	Healthy		Sick				Seriously ill		
Leadership	Search for excellence						Crisis management		
	Prophylactic management			Bad leadership					
				Crisis in leadership					
Decision making	Own decisions			Confusion		Chaos		Foreign decision	
Crisis	Status without crisis		Actual yield crisis			The true nature of the crisis			
Viability	On its own strength				Critical	In decline			
	From the proceeds		From current assets						
Competitio n	Able					Incapable			
Findings	Able to compete			Capable of limited competition		Unable to credit			Insolvent

**Fig. 4.12** Overview of possible states enterprise, including the characteristic znakov [130]

The change of the company status, from a healthy company to a company with troubles is characterized by the associated changes, which occur in this process in terms of

activity, status, value, viability, competitiveness, skills, decision-making and the suitability of management. To identify the real problems, which may lead to changes in its functioning it is really a challenging activity, which should be directed on all of the areas in which the corporate crisis could occur.

#### **4.3.1 The financial crisis of enterprise**

The causes of the company financial difficulties can be very diverse. Nevertheless, the management of the enterprise is responsible for such management, which prevents the formation of unwanted internal reflections and ensures the business against the unexpected external changes.

The financial problems of enterprises can be of varying intensity. According to the degree of the severity of the financial problems of enterprises can be divided into three groups:

- ***Insufficient profitability***, which arises when the rate of capital return linked in the company falls below the normal level in the business field given.
- ***The relative illiquidity or insolvency***, which means that the company is unable to pay its obligations on time. Insolvency may occur in the enterprise:
  - **Temporarily, short-term**, if the company inability to pay is due to some unrepeated adverse cause.
  - **Chronically, long-term** if the company is not longer able to produce sufficient funds by its normal activity to settle down its liabilities. Chronic insolvency of the companies occurs in two forms, such as:
    - *Initial insolvency*, occurs when the amount of on time defaulted company receivables is lower than the sum of time its defaulted obligations. Businesses, which are in the primary insolvency, evoke the insolvency of its suppliers and creditors. This may give rise to a chain of defaulters.
    - *Secondary Insolvency*, which arises when the amount of claims outstanding at the time of their enterprise maturity is higher than the amount of its liabilities outstanding at the time of their maturity. This means that if the borrowers were paying in a timely manner, the company would be able to pay its obligations on time, or would he still remained available liquid resources.
- ***Absolute illiquidity, insolvency or prolongation*** which occurs when the company's obligations are higher than the fair value of its assets. In practice, this means that the company has used the entire equity, and therefore owes more than it owns. The company prolongation is not obvious from the balance sheet, if the fixed assets are expressed in procure prices and receivables at a nominal value.

#### **4.3.2 Information crisis**

When the crisis occurs, it is necessary to provide full information of all interested individuals and groups about what is happening in the company. It is necessary to adopt a common approach to dealing with the press and public, rather than confront the attitudes.

Most enterprises are currently able to collect information and register them, but only few companies are capable to efficiently sort them out and filter them, so that everyone gets the information needed fast, regular, timely and absolutely necessary. An essential factor for to assess the importance of their division is as follows:

- **Information** the company has to collect and provide compulsorily, **by law**. They include:
  - information necessary for the compilation of financial statements,
  - statistical information required by law,
  - registration information of a different nature, whose absence may compromise the legal status of the company, or compromise it in any way.
  
- **Information** whose availability strengthens its position on the market and increases its competitiveness. To this category belong:
  - information about demand development,
  - information on competitive activities,
  - information constituting the database of customers,
  - information about the sales and financial performance of individual products,
  - information about assortment classification and inventory turn,
  - information on claims and payments,
  - information providing a detail analysis of variable costs according to single products,
  - information providing a detail analysis of fixed costs.

The above categories of information can be considered as essential and priority information for successful business management. Other information is mostly minor in nature, nevertheless, it can be interesting and beneficial for the enterprise.

**Marketing information system** consists of two groups of information:

- External information, which consist of:
  - **Database of customers** with identification data, a list of contact persons, their ability to pay, customer's perspective, potential volume of sales, relation to competitors, needs, changes in management, expansion plans, products which they have in the assortment, and other information to illustrate a comprehensive picture of the customer.
  - **Database of competitors** formed by the same data as the customers, which is complemented by interesting product parameters, direction of innovation strategy, changes in capital structure, expansion plans and their funding, personal data of the sales team and marketing department members, size of the marketing budget and other information from which it is possible to determine the intentions of the competition in different time horizons.
  - **Statistical data** related to the subject of company business and all the industries they make or influence the market for the enterprise's products, and other statistical data

affected by the developments in the economy. If the company is active on foreign markets, it needs the same information on these foreign markets. for more information.

- **Market research** formed by systematic registratzion of the results of any market surveys carried out by specialized agencies or businesses.
- Internal information, which are made up of:
  - **Sales and financial assortment performance.**
  - **Database of prices** comprises all price changes of the company's products as well as the competitive prices in detailed assortment calssification on all distribution levels.
  - **Financial statements** presenting the basic orientation map for the executives. The reports must be available on a regular basis and any time interval any detailed assortment classification. The data are reported for periods of current and previous years and the plan for the current year in order to make an immediate comparative analysis.
  - **Sales in territorial configuration**, as well as according to the customers and customer groups.
  - **Sales and productivity gains per customer and product**, it is a special set that forms the intersection of two previous reports and allows controlling the sales and productivity gains for one customer in a complete or selected assortment classification, as well as by individual assortment items to check the sales and productivity gains with all customers who purchase this item.

#### **4.3.3 Crisis communication**

Communication is an important part of managerial function. Without it, the managers cannot affect the individuals and groups so that by its performance they can achieve its performance targets. Long-term success in communication requires from the senior managers:

- Commitment openly communicate and participate in public relations.
- Maintaining a competent communications consultants.
- Incorporation of the strategic communication perspective and public relations in the enterprise development.
- Two-way communication with internal and external audiences.
- Coordination of what is done and what is said.
- Clearly define the goals and objectives of the enterprise.

When the crisis occurs, it is primarily important to **separate formal and informal internal communication flows** and during the crisis not only control them, but also complement the appropriate information. With the first signs of crisis in the enterprises at first informal communication flows are activated, which are preferred by the employees. Even under normal conditions, there is the employees' tendency to mix speculation with reality. In the crisis situation it even escalates. If these signals become unnoticed, they can become a risk for the management. Amount of uncontrolled, distorted, emotionally motivated information

and speculation may prompt the formation of panic or mass psychosis and become an obstacle in the rational management of crisis situations.

It may happen that due to poor communication strategy and inadequate communication tools the companies lose its credibility and formal communication flows and thus free the informal communication flows.

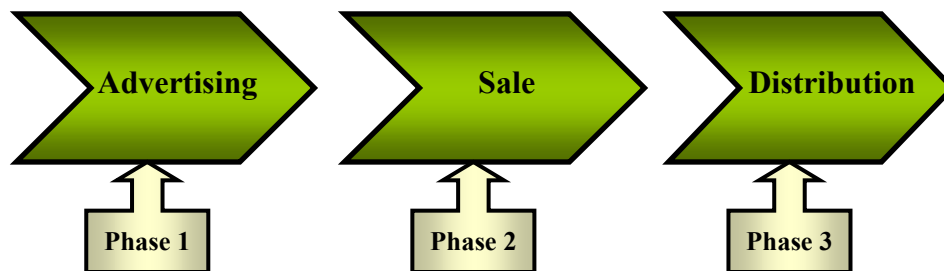
#### **4.3.4 Marketing crisis**

Integration into marketing activities and business organization as well as into thinking of its staff, is the key in achieving such a company this response that ensures permanent advantage over competitors.

Part of the corporate strategy must be not only a marketing strategy, but also an innovation and technology strategy, which result in products related to the trends in demand and financial strategies, which in advance provides financial resources.

Future products development requires close collaboration of marketers, developers, and production and financial management. The product parameters are a very effective tool of the marketing strategy. Its deployment, however, requires a great advance.

One manifestation of the company crisis is represented by the decline in sales of products and services. The reasons for the decline in sales volume may be different. Most often the decrease in sales volume justifies the decrease in demand or insufficient or ineffective advertising. The process of placing the products in the market cannot be limited to advertising, because the whole process takes place in three stages as shown in Figure 4.13.



**Fig. 4.13** The process of placing the product in the market [17]

##### **1. phase – Advertising**

The role of advertising is to reach the target group of customers or target market segments. The purpose of advertising is to draw attention to the product, company, business proposition, generate interest, create awareness among customers.

##### **2. phase – Sale**

In the process of selling, the holder deals directly with the demand carrier. The communication with the customer focuses on appealing to one of the motivating factors for buying applied to a particular customer.

At the stage of sales the communication plays an important role, and its mission is:

- motivate distributors and traders, include the product in own product range,
- check the product for different levels of distribution inventory level,

- take care of appropriate products visibility at the point of sales to the end customer,
- provide sufficient professional information about the parameters of the product.

### **3. phase – Distribution**

The purpose of the distribution is to make the actual physical product closer to the customers and enable their to carry out their intention to buy the product physically.

In the third stage the decision on choosing the strategy which is implemented as follows:

- **Push strategy**, in which the role of advertising is to ensure pulling the product through the distribution network via the interest of customers requiring the product.
- **Pull strategy**, in which the product is pushed through the distribution network away from the producer to the end user, supported by strong advertising.

For the successful sale of the product all three stages of product placement in the market are needed. The individual stages differ significantly not only in the **nature of activities** which present content, but also the **amount of costs** necessary to implement them.

The advertising and distribution are essentially fixed costs that are not directly affected by the actual volume of products sold. Most businesses spend for these two stages of the product placement on the market high amounts of financial means. The measurability of advertising effectiveness is difficult.

Insufficient attention is paid to the **sales stage**, in which there is a buying decision. This stage is largely associated with costs that are variable in nature and the amount depends on the magnitude of the actual sales volume. The effect of sales may be quite easy to quantify. Therefore, **this stage is the least costly**. The sales is the cheapest tool of the marketing strategy, and therefore, it requires adequate attention. The advertising which is not followed by the sales is useless. Likewise, full stock of products do not increase the sales volume without a corresponding sales efforts. The sales is a quite cheapest tool of the marketing strategy. Therefore it is necessary:

- Compare the costs of the sales department to the advertising costs and distribution.
- Carry out a thorough audit of personnel and physical equipment of sales department.
- Confront the audit results with the opinions of the sales department members.

The successful and efficient functioning of the sales can be managed by certain regularities, which are reflected in the way the organization works of all activities related to the sales. Unlike other enterprise activities, the sales activity is a company with which the customer comes into direct contact. The customers can immediately and thoroughly assess the quality and effectiveness of sales based on their own experience. The sales department has to work flawlessly, regardless the quality of the processes that take place in the company and cannot be directly seen by the customers.

The activities carried out within the sales can be divided into three categories:



- **Sales representation** is an activity carried out by sales agents who are employed by the company, or work as salesmen. The sales agents work in a corporate environment and are responsible for:
  - maintaining the contact with existing customers,
  - finding new customers,
  - obtaining information on competitor activity and developments in demand.
- **Sales administration** represents an activity comprising the activities related to:
  - taking orders,
  - dispatch orders,
  - billing,
  - controlling of collection,
  - controlling of inventory.
- **Sales and after-sales service** provides customers with technical assistance to:
  - installation and commissioning of the delivered products,
  - operator training,
  - complaints repairs,
  - providing regular technical maintenance,
  - current and general repairs.

From the calculation, it is clear that the sales includes a large number of activities that need to be managed centrally in order to guarantee a high standard of their implementation. For the long-term survival of the company it is essential that the ***sales activity in the highlight for the senior management***. The functionality of the sales department represents the criterion for the customer to assess the enterprise functionality. Therefore, it is essential that the senior management harmonizes the organization of all enterprise activities.

Care for customers is an important marketing tool that can distract the company from the crisis, or lead it out of the crisis. Maintaining the customer goodwill has its own patterns and system:

- Monitoring the news on a regular basis, in advance, before their official publication.
- Information about the upcoming price changes.
- Assembly, guarantee service and promotional service.
- Brochures and promotional material.
- Responding to emergencies.
- Courtesy visits.
- Regular verification of customers' satisfaction.
- Being free of trouble.

Regular contact with customers is the basic approach, which aims at retaining the customers. The customers expect that the company's interest in them does not end at the moment of signing the order, but that it lasts. If the customers believe that the trading with the company is smooth, their loyalty to the company is greater. Therefore, it is necessary to pay more attention valued customers. To determine the significance of individual customers we can use various methods such as the ABC method, Pareto rule, and the like [17].

#### **4.3.5 Logistic crisis**

Due to the errors of the management and the decreasing turnover, there is the fact, that the stocks comprising raw materials, finished products or semi-finished products in manufacturing are too high when compared to the turnover. The key issue is often not the high inventory itself, but the fact that some items are not available at all, and others are available in surplus quantities which unduly bind the funds.

Under normal conditions, it is possible to achieve the reduction in inventories by up to 20 % by improving the leadership, changing the shopping process, inventory control, production planning and control. If the crisis is caused by large stocks, the company has first take the steps to improve the situation, which may temporarily cause an additional increase the inventories in value terms.

#### **4.4 Stabilizing the crisis**

The next step of the crisis examination is to determine the process by which the enterprise realizes that it is in crisis and adapts to the changes. This distinction is vital because it differs the unforeseen and unforeseeable crisis completely from the creeping, threatening crises which are not publicly known, however, which are already suspected, realized and felt in the company. The examples include financial problems and related facts and figures, to be published in the annual report at the end of the year.

		Reaction enterprise	
		responds	doesn't respond
Awareness of corporate crisis	Yes	The enterprise is aware of the crisis and responds to her	The enterprise is aware of the crisis, but it is not responding
	No	The enterprise unaware of the crisis, but it responds	The company crisis not realize or does not respond to it

**Fig. 4.14** Response to a corporate crisis [107]

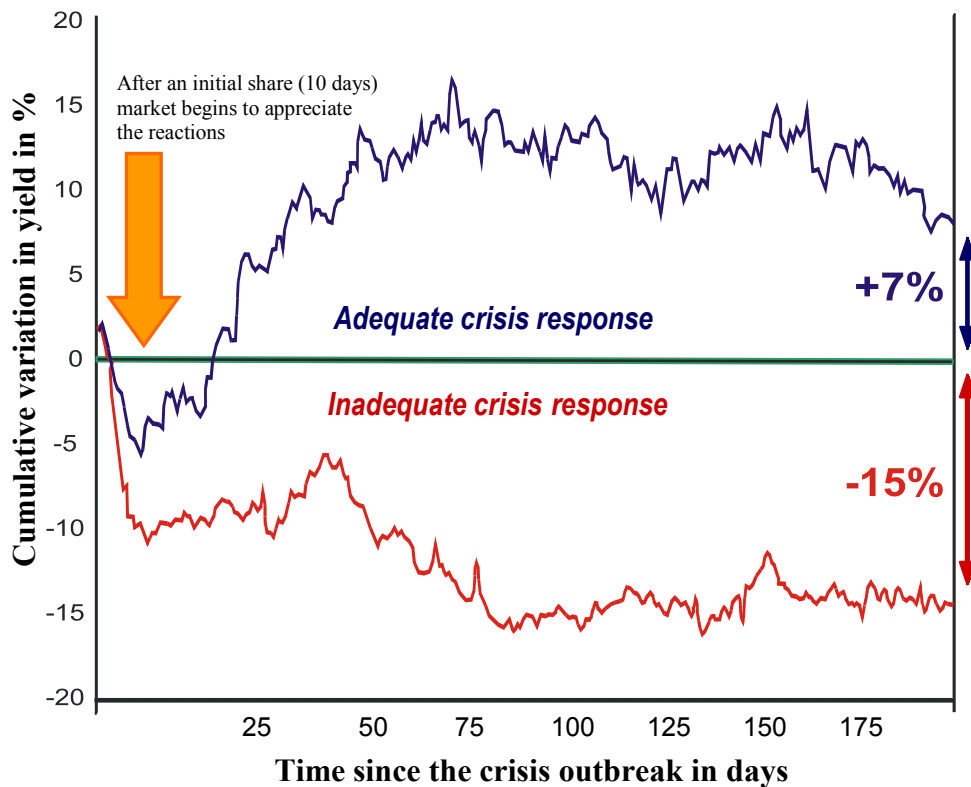
The previous Figure 4.14 provides an overview of possible reactions to the crisis, which then gives rise to the possible ways of its solution.

The rescue the troubled businesses we can use the tools and methods that are available and are widely known. The difference is that these tools and methods should be used under difficult and demanding conditions than during the regular activities. The right choice of priorities is decisive and the secret to success is hidden in the intensive work. The analysis of the existing company state has a classic course:

- Detailed company analysis and diagnosis of its deficiencies.
- Setting goals and priorities, which do not exceed the capabilities of employees.

- Necessary measures and their implementation at all levels, in particular in the management of the enterprise.
- Time-consuming and intense work in very adverse conditions.

Reactions to this crisis phenomena in the company affect the value of the company (Figure 4.15).



**Fig. 4.15** The impact on the value of the company's shares

Responding of enterprises to the state of crisis has its short-term but also long-term impacts. The most dynamic effect is undoubtedly the impact on the shareholders' equity. The study, carried out at Oxford University in the years 1980–1995 evaluating 15 major corporate crises reveals that despite the various causes the crisis differed in their very nature, having a surprising impact on the change in the share price.

The enterprises that effectively cope with the crisis management, the following year recorded the growth of their shares by 7 % in average. In contrast, shares in companies in which the crisis management failed, the shares prices fell by 15 % in average. There was also the damage to the brand name used.

#### **4.4.1 Measures to stabilise the corporate crisis**

Measures aiming at the stabilisation of the company can be divided into:

- **Short-term measures** – „crash programme“ designed to overcome the liquidity crisis.
- **Long-term measures** that lead to long-term ability of the enterprise to remain on the market, stand the competition and make a profit.

It should be stressed that in any case the adopted and implemented short-term measures must not be in conflict with the long-term strategy of the company.

The first step to solve the crisis is to apply emergency measures by which the company gains time. These are the measures that ensure fast and efficient improvement of liquidity and are primarily focused on own business activity. The necessary measures must be implemented as quickly as possible, because the difficult financial situation of the company is rapidly deteriorating and transferred to other areas of the company. At the beginning of the solution the crisis must be addressed to:

- ***Increase in revenue***, which is the easiest to implement by the increase of the products and services prices. Even a small increase in sales prices results in a substantial improvement in earnings and liquidity. The change in prices should be supported by the price calculation, which takes into account the real situation in the company and the market. The calculation of prices has to consider provided rebates, discounts and promotional prices.

Whereas the amount of the price of goods and services is determined by the level of demand and supply, a special opportunity to overcharge occurs at the emergence of an excessive demand for a particular product, for replacement parts and obsolete spare parts. On the supply side, it is possible to improve the sales policy. A flexible remuneration system vendors can reduce net prices.

Last but not least, when considering the change in the prices of goods and services it is necessary to compare the company prices with the prices of the competition and analyze the possible reaction of the competition to own changed prices and price policy.

- ***Reducing costs and losses***. The significant potential to reduce costs are indirect costs, which should represent the first area of cost reduction, on which the company management should focus. The indirect cost savings can be achieved relatively quickly and without affecting the environment of the company. In some cases it is better to completely remove the indirect costs, than just reduce them. In reducing the indirect costs the **strategy of a symbolic sacrifice** is proven, when it is necessary to renounce all luxury spending, but also some necessities. The symbolic sacrifice on the company side has often a positive effect on employees. The actual impact of such a sacrifice at the expenses is less important than the psychological effect, which highlights the seriousness of the situation in the company.

Another item costs, on which the company should aim at are represented by wages and and personnel costs. Dismissal should be approached cautiously, so that the company does not dismiss its best and brightest employees. There should be no mechanical reduction of the workforce.

It is important to analyze the high fixed costs, which are usually contractually agreed costs. The possibility of reducing these costs depends to a certain extent on the managerial skills and competencies and, in particular, on the art to negotiate.

In reducing the direct costs, it is necessary to proceed with caution, because an inappropriate interference into their structure may affect the long-term prospects of the enterprise by disrupting the production, reducing the turnover and discouraging the customers. The long-term disruption of the company activities aimed at achieving short-

term cost savings, are not desirable. The direct costs are reduced only after the value analysis is done thoroughly.

- **Reduction of obligations** is implemented according to the proven obligations control system governed by the following principles:
  - Compile a list of all open obligations.
  - Another obligation is not permitted without a written consent.
  - No written consent is permitted without a signature and without the consent of senior officials at the highest level, with the highest responsibility.
  - Copies of orders must be submitted to the central control where the official concerned has the right to confirm the order or return it.
  - New orders can be confirmed only if they meet the business plan and budget liquidity.

The employees concerned must have defined powers within their field of activity for which they are responsible, including control orders. In the recovery, the company should not overlook the strategy of preferred purchases when buying and must use it. The strategy is based on buying in bulk, shopping discounts, central ordering, credit terms, and the like.

- **Improvement of liquidity** is based on the development of high-quality liquidity budget, which shall include all expenses and income of the enterprise. It is possible to improve the liquidity by:
  - Accelerating the collection of receivables, where it is possible to apply:
    - discount for prompt payment,
    - payment in advance and in cash,
    - telephone or personal intervention by a company management member,
    - development of favorable long-term relationships with the customer's paying department.
  - **Slowing down the settlement of obligations to the contractor**, considering the possible responses from the suppliers. It is necessary to comply with the contractual periods of maturity.
- **Cancel the investments**, with the exception of the vital investments that are short-term investments for the proportional increase in profit, or the investments for the purchase of necessary spare parts. The projects, whose implementation should increase the profits in the long term, may be carried out after overcoming the crisis of liquidity, as a part of long-term planning.

#### **4.4.2 Strategies to stabilize the corporate crisis**

An important step in the management of the corporate crisis is not only to determine the processes by which the company realizes that it is in crisis, but also the processes by

which the company responds to the crisis and adapts to the need for change. This distinction is vital, because it differs the completely unforeseen and unforeseeable crises from the creeping, threatening ones to which the public does not react, which are even publicly not acknowledged, however, which are already suspected, realized and felt inside the company.

The analysis of the business environment and the state of the company on the one hand, and the future state vision and setting the goals of competitiveness, on the other hand, determine the strategic corridor for the selection of procedures. Generally, there is a broader set of reference policy options to transform the company from the unsatisfactory situation in the consolidated and subsequent developing state. The strategic approaches mainly concern the changes in the production capacity, the type of a competitive advantage, diversification of production and access to innovation.

### *I. Changes of productive capacity*

- **Controlled reduction of production** is efficient if the bottlenecks are eliminated in the production cycle, loose material resources are reactivated and savings in workforce allows a significant increase in the labor productivity. This strategy is frequently applied and its potential is generally already exhausted.
- **Elimination strategy** supposes the sales or hire, or complete cessation of some company operations. The strategy relies on having an investor who would be interested in resources released
- **Strategy of total reengineering** assumes the reconstruction of operations via high investments to qualitatively new level characterized by new sophisticated products manufactured by means of advanced technology. The strategy is applied especially in the case of takeovers by foreign investors.
- **Strategy of production increase to the level of capacities and quality improvements**, this is a strategy type of using the company knowledge as well as production potentials, and by medium-sized levels of investments for the selective oriented innovations into promising directions.

### *II. Type of competitive advantage*

- **Cost leadership strategy** is based on universal principles that are represented by low costs. It competes with the price advantage which is achieved by the serial production, efficient organization of processes and cheap inputs. Currently, this is the priority strategy applied.
- **Strategy of differentiation** is based on unique products and quality. The manufacturer ensures the differentiation by providing a strong innovation development and market position. Currently, Slovak companies can apply this strategy only in a limited way.
- **Strategy of concentration** is based on the producer's ability to adapt to its customers, with which the company has long-term partnerships developed. This strategy is applied by the suppliers of components and subsystems in the supply chains.

### *III. Level of specialization*

- **High specialization of products and markets** – limited range of production and operation in a limited market segment enables the high productivity, quality and efficiency. There is

the market risk when the market conditions change and the new technologies emerge. The strategy is particularly efficient when entering the supply chain of a global nature.

- **Diversification of products** – the company provides different products for different markets. The advantage is represented by the ability to compensate the market turbulences. High demands for innovations is the disadvantage. The strategy applies particularly in customer-oriented companies.

#### *IV. Innovative practice*

- **Continuous improvement** – the development is ensured by the sequence of smaller rationalization and innovation projects. The benefits are reinvested in the further development. The advantage is represented by a low risk and lower one-time investments, a long time to achieve growth objectives is the disadvantage.
- **Innovative leap** – provides the introduction of new production programmes based on investments with a qualitatively new level. The premise is generally represented by the transfer of knowledge and innovations, and building the partnership cooperation of businesses, universities, innovation centres and the like.
- **Transformation of strategy into implementation projects** – within reengineering projects the following methodology for the specification of implementation projects is proven:
  - distribution of projects on cross-cut and process-oriented,
  - determine the project priorities, which is important in deciding on the implementation under the conditions of limited resources,
  - allocation of projects to time series,
  - specification of the procedures of the management and projects monitoring [86].

#### **4.5 Solution to the crisis**

If the symptoms of an impending crisis in the company or even the state of crisis are found via the diagnosis, the crisis management formulates the measures in the form of:

- **search for enterprise rescue,**
- **liquidation of enterprise.**

The intensity of the action and measures taken by the company to deal with the crisis, must correspond with the severity of the problems in the enterprise. In principle, they can be divided into:

- **Informal measures** taken by the firm itself usually in cooperation with creditors or with the assistance of counseling organizations.
- **Measures carried out under the supervision of the court** and in accordance with applicable law.

The various methods of dealing with the crisis in the company, according to the implications for enterprise and application of judicial or extrajudicial procedures are shown in Figure 4.16.

	rescue procedures	destructive procedures
informal measures	<b>consolidation</b> <b>remediation</b> <b>out of court settlement</b> <b>restructuring</b> <b>reengineering</b> <b>business combinations</b>	<b>preventive disposal</b> <b>disposal</b>
measures under court supervision	<b>judicial restructuring</b>	<b>competition</b> <b>judicial restructuring</b>

**Fig. 4.16** Methods of dealing with corporate crises

The task of corporate crisis is to recover the business and ensure the further existence of the company in the future. The essence of the life-saving techniques is to get the business under control and manage its cash flows, in order to minimize the negative and maximize the positive cash flows coming into the company. These methods can comprise the following remedial treatments:

- Methods of company rescue without its legal and property demise, which include consolidation, restoration, out-of-court settlement, restructuring and reengineering.
- Methods of company rescue resulting in the legal and formal demise of the company and includes company combinations.

In the market economy it is a frequent that the company gets to the stage when it ceases to prosper, it means that its value declines. It is no longer the one who produces the value, but destroys it. The bankruptcies are an essential part of the market economy and fulfill the several functions:

- for inefficient enterprises they represent the mechanism of market output, and consequently, the transfer of resources to the new activities,
- for some enterprises they represent the mechanism of market output, and then the transfer of resources to the new activities,
- for some troubled enterprises they represent a recovery mechanism,
- for the creditors they represent the mechanism of implementation claims.

**Destructive methods** of dealing with the corporate crises lead to the liquidation of the company. They lead to the demise and settlement of its legal and financial relations. By the liquidation of the company means the cessation of its activities and its subsequent dissolution. The causes of disposal may vary. Generally, it is possible to speak of liquidation in the following form:

- forced, if the enterprise is bankrupt,
- on its own decision, if the enterprise fulfilled the aim for which it was created.

#### **4.5.1 Consolidation**

**Consolidation** is carried out through the development consolidation programme. The business objective, scope and organizational structure in the company are maintained.



Usually, the company management, management work style, control methods are changed and economical measures to improve performance are looked for. This is a relatively gentle way to save the company, which is implemented by specialized consulting firms. The consolidation is usually concealed from public, so that the company does not lose confidence of its business partners.

The consolidation should be carried out in the following steps:

1. **Analysis of the enterprise'evolution** via financial-economic analysis methods. The ex-post analysis is used for the evaluation of the absolute and relative indicators, which are compared with the average values of the indicators in the sector.
2. **Revealing the causes of difficulties** because of their formation and persistence. The individual sub-problems that need to be addressed are stipulated.
3. **Proposals to address the troubles** that may relate to technical, logistical, informational, organizational, sociological, financial and other areas.
4. **Implementation of the consolidation process**, which is extremely difficult because it work during the normal business operation. Usually, the company achieves better results if they are ensured by an external team.

Consolidation measures may be generally focused on three sets of activities that are interrelated:

- **Stabilization or increase of business turnover** by adjusting the production structure, changes in business strategy, and the like. This reduces the market risk of the company. Achievement of this goal usually requires additional resources and time.
- **Reducing costs**, primarily of fixed nature, which constantly lay burdens on the business. It improves the profit of the company and reduces its sensitivity to fluctuations in sales.
- **Measures in finance**, which are designed to adjust the volume and structure of corporate assets and capital. The adjustment to the business assets is aimed at the increase of its liquidity, which is then used to pay the corporate obligations, thereby reducing the total amount of committed capital, improving the financial structure, reducing the debt service and increasing the credit rating of the company.

Consolidation measures have to be assessed comprehensively and their side effects have to be taken into account as well. It is necessary to continuously evaluate the implementation of the consolidation programme in accordance with the desired results.

#### **4.5.2 Remediation**

Remediation is a difficult rescue operation, which is usually located in a deep crisis and diagnostics indicates a number of "unprofitable outbreaks" that have to be removed. Only the "hard core" of the company which produces no loss is retained. Unlike the consolidation, the remediation releaves only those functional departments that produce no loss and all others are disposed of. The successful remediation averts the decline and demise of the business.

***Remediation** is a package of measures to overcome the longer duration of loss in the company or its long-term insolvency. Its aim is to save the enterprise prior to its liquidation.*

The remediation is always a drastic intervention in the business venture. In its planning and execution an independent view of the firm, which is not affected by the corporate blindness is preferably used. Therefore, the in the remediation of larger companies utilizes the services of counseling agencies.

If the analysis of the causes of the company critical state shows that the company can be saved, the remediation plan is developed. The first step in the remediation is usually represented by the change in the corporate management, which includes the appointment of the crisis management. The remediation programme is based on defined objectives:

- Regarding the strict selection, keep only the most vital company parts. In accordance with this order the organizational structure and system of powers and responsibilities are regulated.
- Acquire quick cash via different forms.
- Form time space for the remediation programme implementation, for example, by the agreement with business partners and banks to postpone the payments.
- Radically minimize the costs and achieve a turn in profitability.
- Obtain additional financial sources, thereby prolonging the time for the recovery process of the enterprise.
- Implement an effective communication policy aimed at convincing the business partners, banks, lenders and the public that measures the enterprise has already overcome the greatest risks.
- Stabilize the profitability and direct the enterprise to its further growth.

For the recovery process, the company can use the following forms of remediation:

- **Net remediation** aims at covering the losses from corporate venture capital. As a rule, the capital is reduced by an amount greater than the reported loss, so the simultaneously the reserves funds are formed strengthening thus the company's financial position. The disadvantage of pure remediation is that it does not bring additional liquidity means to the company.
- **Remediation via acquiring new resources from owners** that do not increase the basic capital of the company, but pay the loss and become a part of its capital. The additional resources from the owners provide the liquidity means to enable the implementation of the file remediation interventions. This form of remediation is based on voluntary individual owners who cannot be compelled to provide additional sources.
- **Remediation via adjusting the payments** to creditors may take various forms:
  - Agreement with creditors to postpone the maturity of certain corporate obligations.
  - Change of part of short-term liabilities to the medium or long-term liabilities, such as obtaining medium-term credit, of which it pays back the short-term credits or issuance of corporate bonds.
  - Agreement with creditors to forgive part of the liability.
  - Capitalization of liabilities in the form of conversion of the creditor to the co-owner, e.g. via the corporate bonds in exchange for company shares.

- **Reduction of capital tied in company with its consequent increase** represents the most favorable variable remediation because its implementation brings additional liquidity to the company allowing thus new investments to remove outbreaks producing losses and implement new business plans. The basic assumption of this form of remediation is to convince the investors about the feasibility and success of the remediation programme.

#### **4.5.3 Out of court settlement**

*Out of court settlement* is an agreement with all creditors on a partial settlement of their claims against the company which is in financial difficulties. The percentage of claims settlement is the subject matter of mutual agreement. The creditors are willing to agree if the intervention of the court in the form of bankruptcy can expect even lower percentage of their claims settlement, and with much later date. This form of solving the corporate insolvency is rare because it requires the consent of all creditors.

#### **4.5.4 Restructuring the enterprise**

*Restructuring* is suitable for businesses which are in debt, insolvent or in loss, whose yield capability can be significantly improved and sustained by the changes in the structure, strategy or costs. It is a process that is largely affected by the quality and consistency of the strategy implemented. Restructuring is the process of overall changes in the company, which are based on the implementation of appropriate restructuring measures.

The restructuring of business processes is a tool that can help the company in crisis situations. It uses the tools and techniques that have cross-functional nature. The restructuring is usually implemented as a remedy. The process starts at the time of the first signs of the crisis or in the process of acute crisis. The sooner the restructuring is implemented, the lower the costs associated with saving the company are. Ideally, the restructuring is implemented as a precautionary measure, and the company receives a competitive advantage.

The essential step in the development of the restructuring project is to identify the purpose for which the restructuring takes place. The purpose of the restructuring in the current period are mainly represented by the following reasons:

- removal of dubious assets,
- optimization of the enterprise value,
- enterprise recovery,
- reduction of costs.

The first step in the restructuring is to determine the extent to which the enterprise is to be restructured.

The main point of the successful restructuring can possibly include:

- understanding the actual situation,
- strong interest in the rebirth of the enterprise,
- definition of priorities,
- establishment of clear objectives and responsibilities,

- gain of confidence,
- constant inspiration and motivation,
- stabilization of achievements.

#### **4.5.5 Reengineering processes**

Comprehensive reengineering includes three levels of the radical transformation of the whole enterprise, which are expressed by concept of "3R":

- **Rethinking** – reflection and finding new meaning and purpose of the entire enterprise.
- **Redefinition** – review of corporate management model based on the process approach.
- **Redesign** – re-engineering of all processes in the company in terms of creating the maximum value for the customer.

*Reengineering as a substantial, dramatic and radical change of the previous perceptions and the organization of corporate processes is the solution aimed at increasing the functional capability of the enterprise considered as an open system of four fundamental aspects:*

- *Component* that determines what resources and what features are required to take the necessary level of functioning.
- *Structural*, which provides how to organize material and information flows among the various processes in order to use the existing company resources optimally.
- *Functional*, which expresses how to integrate individual components and resources into larger units and processes in favour of the lowest possible costs for the performance of the company business activities.
- *Integration*, which determines how to ensure the management of individual processes in the company to achieve the highest possible level of competitiveness.

The reengineering is a fundamental tool for principle organizational changes in business activities Its success is conditional upon:

- **Concept**, vision and strategy of the company, which are necessary to achieve the objectives. The idea is a picture of what is desirable in relation to the people, products, processes, possibilities, and consumer culture. Without ideas the company is indefinite and without a target.
- **Skills**, high skills levels of management and the ability of continuous education, which are necessary to perform the tasks in the new processes. Without these skills, the individuals concerned and do not perform at the required level.
- **Motivation**, which is generally the last unstable element. Without motivation, people do not change, or do only incremental changes. When the motivation changes, the employees find a way to work efficiently in order to pay back for their efforts, and in order the company achieves the desired change.

- **Sources**, which consist of people, finances, information, new possibilities and tools needed to change. Without resources, people who in charge of the changes implementation are disappointed and the expectations to be brought to the enterprise, are unrealistic.
- **Plan of action** that determines the sequence and contents of the individual steps to be implemented.

The objective of reengineering of the business processes in the enterprise is to change the system, so that the new arrangement gives the rise to new entrepreneurial competences of the enterprise as a whole as well as of its individual employees. The reengineering of business processes based on the assumption that the losses and inefficiencies in the implementation of business are caused by the fact, that the managers cannot correctly identify the customer requirements and remove internal barriers for more effective inter-service cooperation. The solution to this situation is to integrate the efforts of all staff in defining and achieving the performance competitiveness.

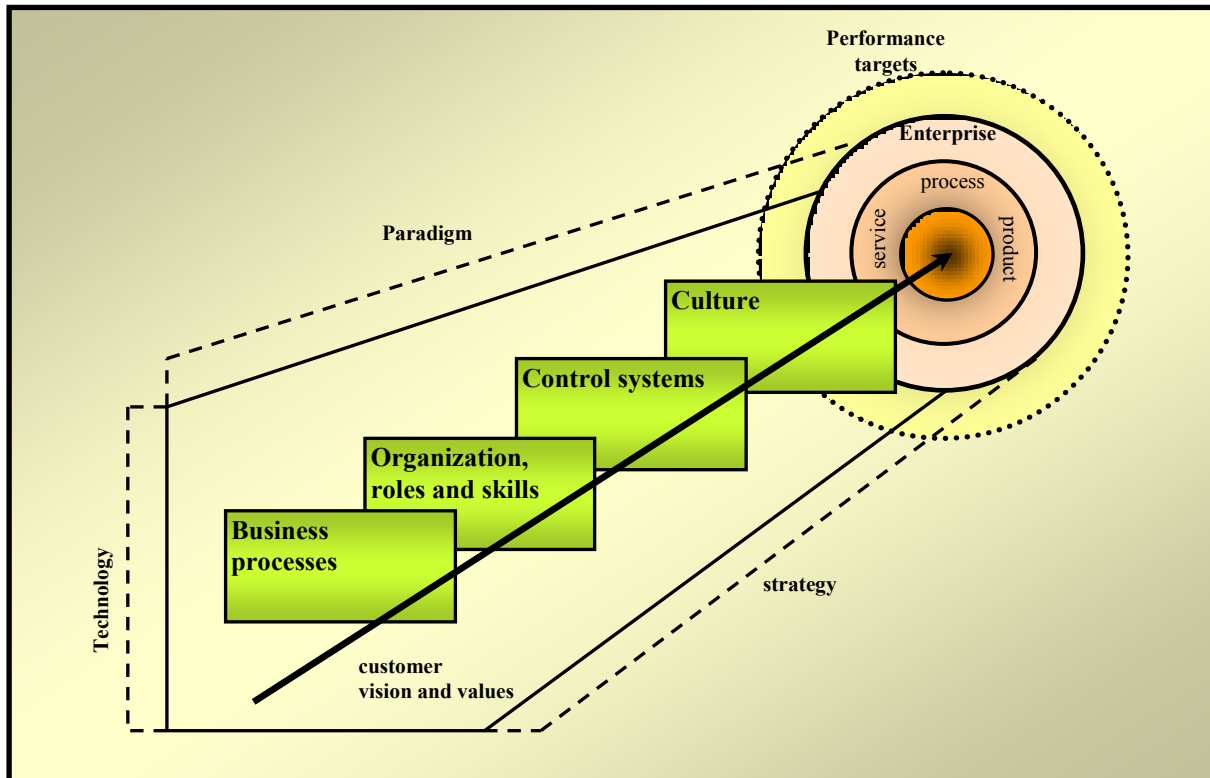
The reengineering focuses on large, cross-cut processes and the entire corporate system. Therefore, the reengineering cannot be initiated and maintained by the middle or lower management. It is entirely driven from the top management by the leader who believes that nothing is more important than the re-engineering, and who is willing to do anything for the reengineering to be successful. Table 4.1 shows the differences between re-engineering and continuous improvement.

**Tab 4.1** Differences between reengineering and continuous improvement of business processes

Parameter	Continuous change	Reengineering
<i>Area</i>	Extensive	Focused
<i>Width</i>	Small process	Large process
<i>Depth</i>	Existing business process	The overall business process
<i>Impact</i>	Style of work	Discontinuity style
<i>Objectives</i>	Gradual 5–20%	Radical least 50%
<i>Leadership</i>	Authorization, support	Contract and direct execution
<i>Range</i>	Evolutionary	Revolutionary
<i>Method</i>	Detailed analysis	Iterative design and testing
<i>Pattern</i>	Complexity and precision	Simplicity and ambiguity
<i>Style</i>	Improve the existing process	Redesign from the beginning towards results
<i>Assumptions</i>	Healthy process	Corrupt process
<i>Methodology</i>	Industrial engineering	Innovation and change management
<i>Technology</i>	Identifying root causes	Breaking the rules
<i>The main idea</i>	Elimination of waste and variability	Information technology as a key means

Comparison of two approaches via the set of 14 characteristics facilitates the understanding of reengineering, as an oriented approach for achieving rapid and fundamental changes in performance.

For successful re-engineering it is necessary to consider the key aspects shown in Figure 4.17. The first step of the whole effort is to focus on the customer. Knowing the customer requirements and market trends we can derive the understanding of the company business process. The requirements for different product features and supply conditions define the parameters of the company business process. In other words, the business process should be arranged so that it is able to meet these requirements at its best. New understanding of the company's mission, goals, business process define the requirements for the organization, role of individual organizational units and skills of managers. The reengineering imposes the substantially new requirements for the enterprise management system and corporate culture.



Aspect	Visible	Invisible
<b>Business processes</b>	Tasks and workflows Services and materials Levels of resources Inputs and outputs	View of the overall process Costs of assets Performance and obstacles Hidden assumptions Value for customers
<b>Organization</b> <b>Mission</b> <b>Skills</b>	Description of the job Names positions Organization chart Saving the tasks in the project Decision-making levels	Current skills Informal influences Informal relations Career Feeling of performance
<b>Management system</b>	Measuring of the effectiveness Feedback efficiency Financial rewards Management practices	Unexpected behavior Effects of feedback Non-financial rewards The paradigm of leadership
<b>Culture</b>	Set resolutions Behaviors and styles Writing, symbols, language	Current opinions Corporate Culture Teamwork
<b>Technology</b>	Features of products and services Cost technology Technology solutions Hardware and software Data, reports and visibility	Competence Know-how Benefits of technology Unknown problems Shadow systems
<b>Paradigm</b>	Decisions and solutions	Rules and systems reviews
<b>Strategy</b>	Business strategy	Strategy changes

Everything within the reengineering efforts is directed towards the achievement of fundamentally new parameters of efficiency within the selected company, via the processes, products and services. All these aspects are modified, within which there are technology development, corporate identity and corporate strategy.

Experience of practitioners in reengineering point out on two groups of specific aspects, to be analyzed, i.e. how the company wants to achieve superior results, in other words visible and invisible aspects, further specified in Table 2.4.

Experience of consulting firms show that the Slovak companies focus mainly on visible aspects of reengineering, which are identified and solved. The ignorance of the invisible aspects and their disrespect, may substantially affect the success of reengineering.

#### **4.5.6 Business combinations**

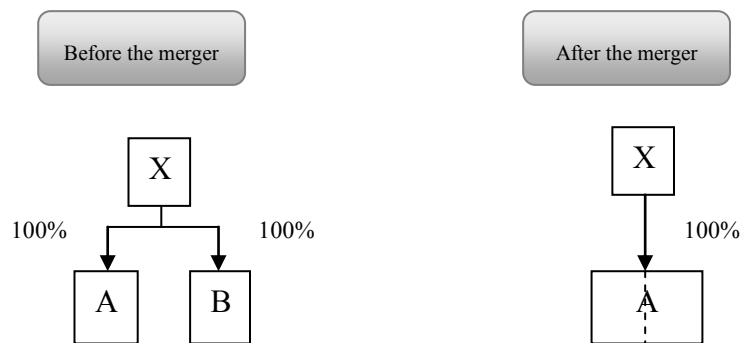
The strategy to handle the company crisis situation includes business combinations, which can be divided into three basic forms:

- merger of enterprises,
- fusion of enterprises,
- division of enterprises.

By the strategies for individual business combinations the legal termination of certain companies occurs.

##### **4.5.6.1 Merger of enterprises**

**A merger occurs** when the merging companies can be expressed as  $A + B = A$ . Company B is merged into Company A, Company B is terminated without liquidation and Company A is the legal successor of Company B.



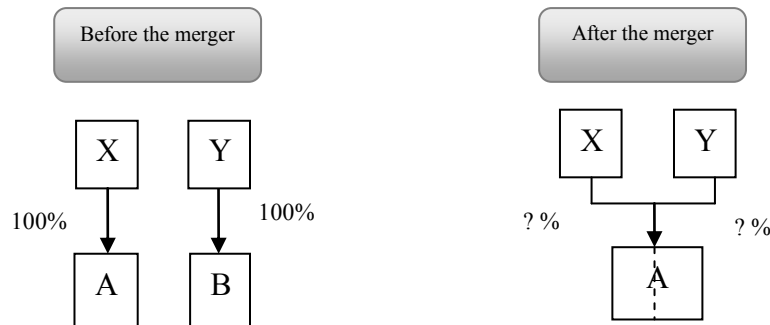
**Fig. 4.18** Merger of two sister companies

Company X has a 100% stake in A and B. Company X is therefore the parent company to company A and company B. Companies A and B are subsidiaries of X company. Companies A and B are therefore affiliated companies.

In a merger according to the scheme  $A + B = A$ , company B merges to company A, company B is terminated without liquidation, and company A is its legal successor. After the merger company X has 100% stake in Company A, Company A is "increased" by company B.

Company X has 100% stake in A. Company Y has 100% stake in B. Company X is therefore the parent company to company A, company Y is the parent company to company

B. Company is A a subsidiary of company X, company B is a subsidiary of the company Y. Companies A and B are not mutually sister companies.

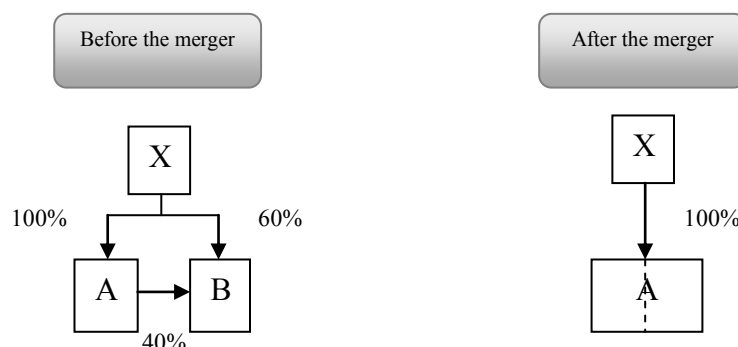


**Fig. 4.19** Merger of two independent companies

In a merger according to the scheme  $A + B = A$ , company B is merged to the company A. Company B is terminated without liquidation and company A is its legal successor. Shares in the company A are the property of company X, but the shares in the company are also the property of company Y as well, even although it has no shares so far. The percentage of shares of X and Y in company A depends on the agreement in the contract of merger. At first glance it might seem that the amount of each share should be 50%. However, this is only a theoretical possibility, because this situation arises only if the value of the company A before the merger is the same as the value of B, which generally is not. The value of the company is not represented by the amount of its capital, however, in practice this sometimes happens, perhaps due to ignorance.

There is also the possibility that some of the companies X and Y, say that company Y is no longer interested in being a partner in the company A after the merger. Therefore, the companies agree, that company X pays to the company Y, or carries out the settlement in other way. After the merger, the company X is the sole member of company A, and company A is increased by company B.

Company X has 100% stake in the company A and 60% stake in company B. Company X is therefore the parent company also for the company A, and company B having here the absolute majority. Companies A and B are subsidiaries of the company X. Companies A and B are therefore affiliated companies. Company A has 40% stake in company B.



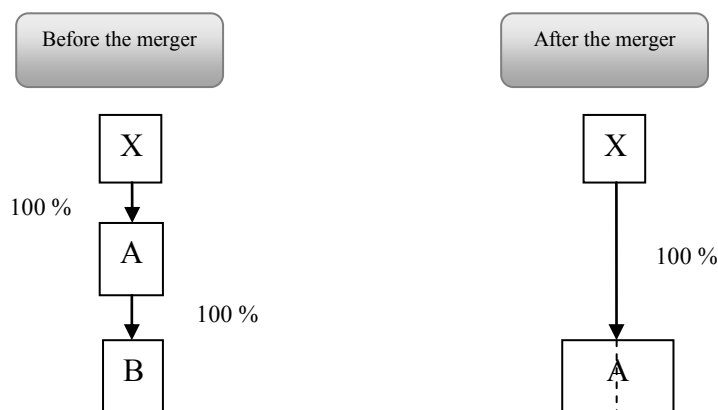
**Fig. 4.20** Merger of two sister companies, one having a share in the other one

In the merger according to the scheme  $A + B = A$ , company B is merged to company A. Company B is terminated without liquidation and company A is its legal successor. After the



merger company X has further 100% stake in company A. Company A is increased by company B.

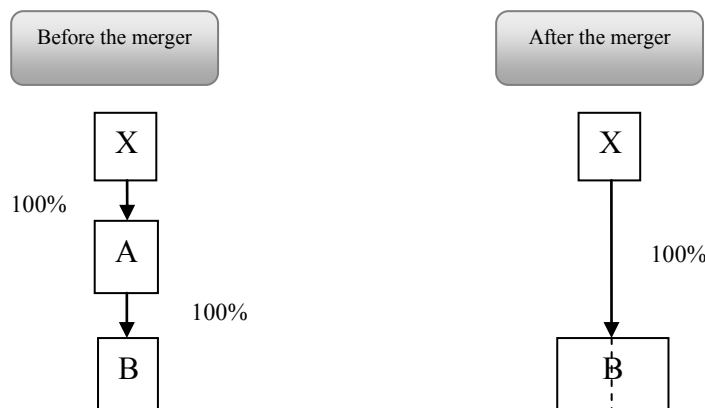
Company X has 100% stake in company A, which has 100% stake in company B. Company X is therefore the parent company for the company A, and a "grandparent" for company B. Company A is the parent company to company B. Company B is a subsidiary of the company A, and a "sub" for company X.



**Fig. 4.21** Merger of the subsidiary to the parent company

In the merger according to the scheme  $A + B = A$ , company B is merged to company A. Company B is terminated without liquidation and company A is its legal successor. After the merger, company X has further 100% stake in company A, company A is "increased" by company B.

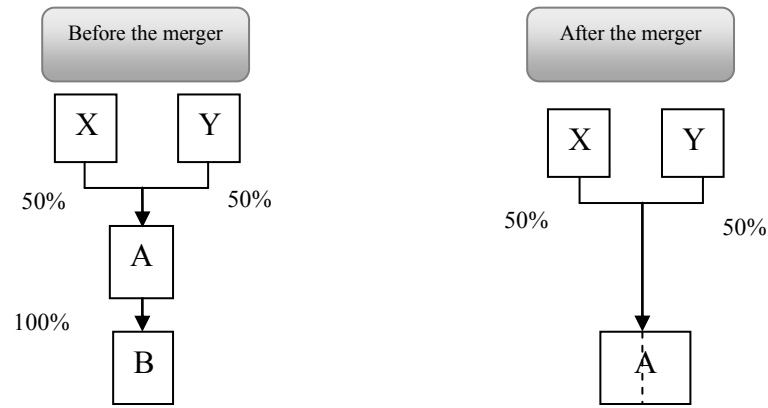
The situation is similar to the previous one, but company A merges to company B.



**Fig. 4.22** Merging the parent company to the subsidiary

In the merger according to the scheme  $A + B = B$ , company A is merged to company B. Company A is terminated without liquidation and company B is its legal successor. After the merger, company X has 100% stake in company B, company B is "increased" by company A.

Company X has 50% stake in company A and company Y has also 50% stake in company A. Company A has 100% stake in company B. Company A is the parent company to company B. Company B is a subsidiary of company A.



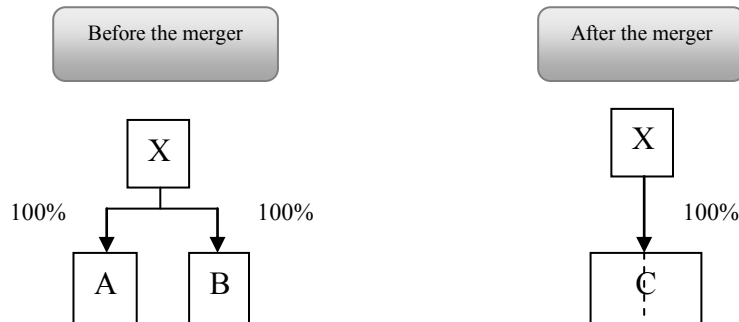
**Fig. 4.23** Merger of the subsidiary to the parent company

In the merger according to the scheme  $A + B = A$ , company B is merged to company A. Company B is terminated without liquidation and company A is its legal successor. After the merger, company X has further 50% stake in company A and company Y has further 50% stake in company A. Company A is "increased" by company B.

#### 4.5.6.2 Fusion of enterprises

A **fusion** occurs when fusing companies can be schematically expressed as  $A + B = C$ , company A and company B fuse into company C; companies A and B are terminated without liquidation and company C is the legal successor of companies A and B.

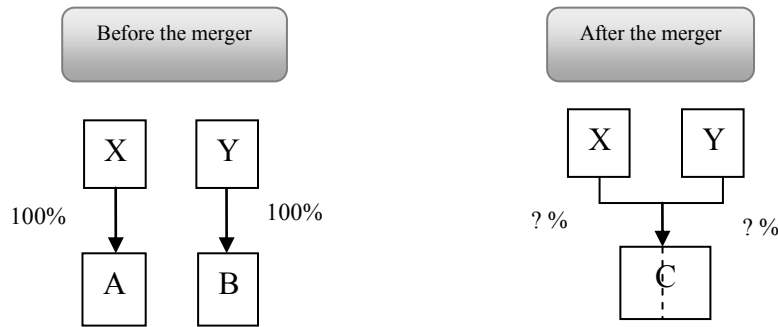
Company X has 100% stake in company A and 100% stake in company B. Company X is the parent company to company A and company B. Companies A and B are subsidiaries of company X and they are sister companies.



**Fig. 4.24** Fusion of two sister companies

In the fusion according to the scheme  $A + B = C$ , companies A and B fuse to company C. Companies A and B are terminated without liquidation and company C is its legal successor. After the fusion company X has 100% stake in company C. Company C is composed of original companies A and B.

Company X has 100% stake in company A, company Y has 100% stake in company B. Company X is therefore the parent company to company A, company Y is the parent company to company B. Company A is a subsidiary of company X, company B is a subsidiary of company Y. Companies A and B are not sister companies.



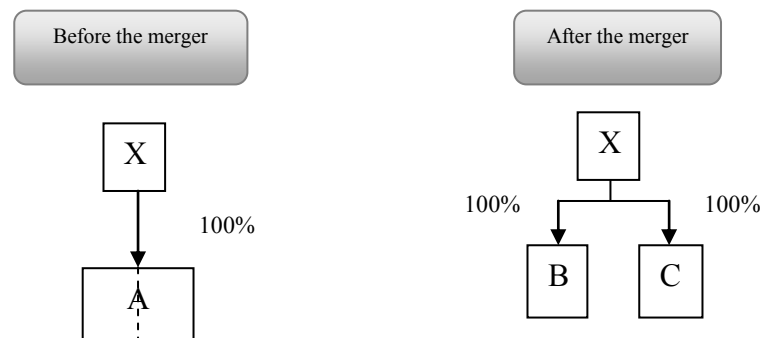
**Fig. 4.25** Fusion of two independent companies

After the fusion according to the scheme  $A + B = C$ , companies A and B fuse to company C. Companies A and B are terminated without liquidation and company C is its legal successor. Shares in company C are owned by companies X and Y. The percentage of shares of companies X and Y in company C depend on the contract on fusion these companies agreed.

There is also the possibility that some of these companies X and Y, for example, company Y is not interested to be involved in company C after the fusion, and therefore, the companies agree that company X compensates company Y, or executes the settlement otherwise. After the fusion, company X is the sole member of company C, company C consists of the original companies A and B.

#### 4.5.6.3 Division of enterprises

**Division** occurs in the division of companies, schematically expressed as  $A = B + C$ . Company A is divided into company B and company C. Company A is terminated without liquidation, and companies B and C are the legal successor of company A; companies B and C are already existing companies, in this case it is the division of companies via the merger, or newly established companies.



**Fig. 4.26** Division

Company X has 100% stake in company A. Company X is therefore the parent company of company A and company A is a subsidiary of company X.

In the division according to the scheme  $A = B + C$ , company A is divided into companies B and C. Company A is terminated without going into liquidation and companies B and C are its legal successors. After the division, company X has 100% stake in the company B and in company C as well.

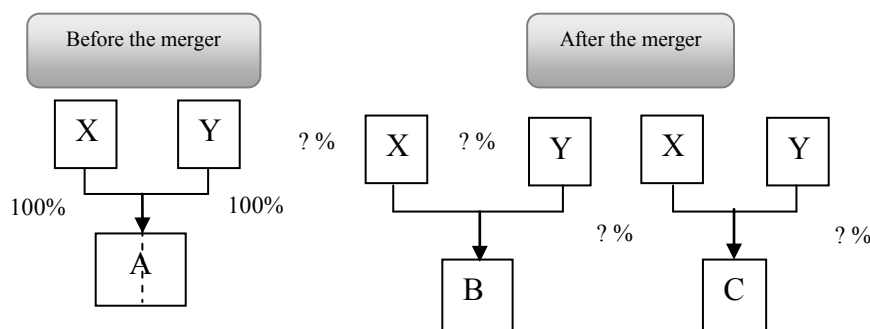


Fig. 4.27 Multiple division

Company X has 50% stake in company A and company Y has also 50% stake in company A.

When divided according to the scheme  $A = B + C$ , company A is divided into companies B and C. Company A is terminated without liquidation and companies B and C are its legal successors. Shares of companies X and Y in companies B and C are agreed in the contract on fusion.

There is also the possibility that some of the companies X and Y, for example company Y has no interest in being a shareholder in companies B and C after the division, and therefore, the companies agree that company X compensates company Y corporation, or executes the settlement otherwise. After the division, company X is the sole shareholder of companies B and C.

If company X and Y agree that company X has 100% stake in company B, and Y has 100% stake in company C, and if the value of B and C is not the same, then companies X and Y compensate each other or settle the difference otherwise.

#### 4.5.7 Judicial restructuring

**Restructuring** is permissible only for the solution of the entrepreneur's bankruptcy, whose business is in operation. It allows settling the debts within the restructuralization only for the entrepreneur carrying out entrepreneurial activity.

In case the firm fails to stabilize and overcome the liquidity troubles, the company gets bankrupt. **The decline of the debtor** is characterized as *an objective condition of the debtor, which occurs independently on the actions of the third parties or the court. If the debtor files for the permission to restructuralize or bankruptcy, it is understood that the debtor is in decline. The business entity is in the decline when it is in the state of:*

- **Insolvency** which is formed by the inability of the debtor to pay at least two financial obligations to at least two creditors 30 days overdue. All financial obligations related to one creditor at the time of the bankruptcy petition and 90 days before that date are considered to be the claim. Such defined obligation has to prevent the formation of ad hoc terms of the decline only by one creditor.

The basis of the insolvency is objective inability of the debtor to pay their outstanding obligations. The failure to pay two outstanding obligations overdue does not automatically represent this strict inability.

According to the nature of causes of the company insolvency there are:

- **primary insolvency**, which is raised by own business activity,
  - **secondary insolvency**, which is caused by the fact that the company is not paid the obligations due by other companies.
- 
- **Prolongation** which occurs when the debtor has at least two creditors, while the value of their liabilities exceed their assets. Only such a debtor who is required to keep accounts pursuant to Act No. 431/2002 Coll. on Accounting can get into bankruptcy by prolongation. This means, that a natural person – non-entrepreneur cannot get into the bankrupt in this form. The value of assets and liabilities is determined by the value of the debtor's accounts [183].

Clear rules for the method determining the prolongation and insolvency are necessary, particularly regarding the obligation of a debtor who is insolvent, had has to file for bankruptcy. The consequences of failure to fulfill this obligation, as well as their right to certify the solvency by the creditor's proposal.

In the insolvency and restructuring proceedings the equality of creditors with equal rights is set. None of the creditors of the claims given has no special procedural status and the legislation directly prohibits their favoritism.

Causes of bankruptcy may be different:

- **controllable by causes:**
  - errors and mistakes in the management,
  - effects of capital, for example dubious receivables, changes in interest rates, lack of capital,
  - operational influences such as obsolete production, loss of production and stocks, inadequate marketing,
  - failure caused by the negative actions of people such as theft, embezzlement, corruption, etc.,
  - employees fluctuation.
  
- **uncontrollable causes:**
  - natural factors, such as fires caused by nature, floods, weather,
  - economic impacts, for example peak seasons' changes, changes in purchasing power, credit, price and supply conditions.

Kinds of causes and scale of their occurrence likelihood are varied, but quantifiable. Almost every unsolved negative effect usually leads to the crisis. The crisis as the culmination of negative impacts, never arises by chance. It has its own inner development and in the environment it strikes, it acts with variable intensity and degrees of severity. If the management fails to deal with some of these causes, as a consequence, the whole enterprise goes bankrupt.

The debtor is required to prevent the economic problems and bankruptcy. If the debtor risks insolvency, s/he is obliged to adopt, without delay, appropriate and proportional measures to avert or solve the situation out of court.

**Decline caused by criminal negligence or malpractice** is an offense falling into the category of offenses against economic and social system. The decline caused by criminal negligence or malpractice, named as fraudulent bankruptcy, threatens not only the assets of directly affected people, but also the system of economic relations in general, and the banking system in particular.

The seriousness of this type of offense is currently growing. That is why most European countries take appropriate regulatory measures. Each of these countries, however, modifies the comprehension of the offense in their laws differently, somewhere it is covered by criminal law, in other countries it is the subject of the separate bankruptcy law.

According to Sec. (§) 227 of the Criminal Code of the Slovak Republic, for the crime **of fraudulent bankruptcy** the person who causes the decline of the legal entity of the statutory case may be accused. And their property, even in part is used to establish the other legal entity, or to obtain its stake in other legal person. Obviously, they must prove the intention to cause the damage, or acquire for self or someone else, an unfair advantage.

Offense of fraudulent bankruptcy is committed also by whoever wants to intentionally cause the decline of the legal person. Penalties are determined by the magnitude of the damage the offender causes. Most severe term of imprisonment of five to twelve years is imposed on whoever by their actions causes the decline to someone else.

**Culpable bankruptcy**, according to Sec. (§) 228 of the Criminal Code of the Slovak Republic, is represented by the bankruptcy of a legal entity, and in the larger extent the failure to satisfy the creditor by that, that without an adequate financial coverage invests in loss-making business, accepts or provides in terms of property options of the legal person a disadvantageous loan, destroys, damages, donates, conceals or otherwise removes a part the property of the related legal person, or uses the greater part of the income from the business of legal entity for their own personal consumption, or places the income from the business of a legal person in lotteries, games or bets. The penalties are determined depending on the extent of the damage that the offender causes, by the imprisonment in the range of one to eight years.

#### **4.5.8 Bankruptcy**

Financial decline of the debtor's is dealt by the **bankruptcy**, if the debtor has creditors and is not able to meet its obligations for a longer time. The objective of the bankruptcy is to achieve proportional satisfaction of the creditors from the bankrupt's assets. After the bankruptcy is announced, the bankrupt loses the right to dispose with the property.

A motion for bankruptcy is filed with the competent court. The bankruptcy motion may be filed by the debtor, creditor, liquidator of the debtor or another person.

**Course of solving the insolvency by bankruptcy** has three stages of the trial:

1. receipt of the motion to the court, when the hearing of the petition in bankruptcy begins, up to beginning of the bankruptcy proceedings,

2. from the commencement of bankruptcy proceedings to the bankruptcy announcement,
3. from bankruptcy announcement to bankruptcy annulment.

Parties to the bankruptcy procedure are: the debtor (bankrupt), plaintiff and creditors who have filed their claims. The bankruptcy starts by the date of making the order for bankruptcy in the Journal of Business public.

The court shall appoint an administrator of the persons registered in the list of trustees, which has established an office in the district of the county court, in which it has the competent bankruptcy court. The manager is appointed on a random basis using technical and programme means.

If the court has doubts in the bankruptcy proceedings about the borrower of wealth, i.e. whether the debtor's assets are sufficient at least to satisfy the claims against the estate, it establishes temporary administrator. If, after the debtor is appointed a temporary administrator, the court in the bankruptcy proceedings finds that the debtor's assets are not sufficient to cover the costs of bankruptcy, the bankruptcy proceedings is stopped for the lack of assets. If the court stops the bankruptcy proceedings for the lack of assets, the effects of the bankruptcy proceedings cease only after publishing a notice of the effective date of the resolution terminating the bankruptcy proceedings for the lack of assets in the Commercial Journal.

In the bankruptcy proceedings, the creditors have the right to proportionally satisfy their claims from the proceeds of liquidation. They have this right only if their claims are properly and on time filed. The law allows the administrator to deny in the claims their:

- legal ground,
- enforcement,
- height,
- ranking,
- ensuring the security right,
- ranking hedging law.

The possibility of claiming the secured liability does not worsen as a result of bankruptcy announcement. On the contrary, following the execution of the inventory, the secured creditor practically decides on the form and time of selling the property part from which they have to be satisfied in an unlimited way.

Contractual agreements prohibiting the bankrupt to delegate their claims or prohibiting the delegation of claims arising against the bankrupt before the bankruptcy announcement, are inefficient during the bankruptcy and the trustee as well as the creditor may delegate these such claims to other persons.

The subject of bankruptcy is:

- property owned by the bankrupt at the time of the bankruptcy,
- property acquired by the bankrupt during the bankruptcy,

- property that secures the obligations of the bankrupt,
- other property, if provided for by law on bankruptcy and restructuring.

The property as the subject to the bankruptcy forms the **bankruptcy basis**, which is divided into a general basis and individual separate bases of secured creditors.

In addressing the bankruptcy it is not the priority to maintain the company operation. Since the opening of bankruptcy proceedings the debtor becomes liable to restrict their activities to only standard legal acts. The operation of the business cannot be carried out at the expense of the bankruptcy yield, it means that running the business cannot be in loss.

The administrator provided for the bankruptcy immediately and with professional care, evaluates the possibility to continue in the company operation of the bankrupt and under the circumstances terminate the company operation, or continues to operate the business. The operation of the bankrupt's company the administrator can proceed only if it can be reasonably assumed that the compensatory transfer of the business or compensatory transfer of all assets or a substantial part of the property belonging to the enterprise with one legal capacity, acquires a significantly higher yield from the realization of the assets belonging to the company, than if they monetize the company otherwise. The business operation must be limited to the extent needed to achieve that purpose.

In summary, it can be said that the bankruptcy announcement has the following effects:

- authorization to dispose of the property passes to the bankruptcy trustee,
- legal actions against the debtor's bankruptcy creditors are ineffective,
- unpaid claims and liabilities relating to the bankruptcy become payable,
- any debtor orders and powers of authorizations cease,
- debtor may refuse to accept the gift or reject the heritage only with the consent of the administrator [183].

#### **4.5.9 Liquidation**

**Liquidation** takes the form of not only formal but also material demise, when its business activities are completely terminated. It comes to the complete demise of the company.

In the liquidation it is assumed that revenues from the sales and liabilities are sufficient to meet all obligations. If in the budget of the liquidation the liquidator finds that the revenues from the sales and liabilities are insufficient to meet the obligations, the liquidator proceeds under applicable legal provisions, i.e. files the motion for the bankruptcy.

Another possible solution to the company crisis is represented by the **preventive liquidation**, which is carried out on the initiative of the owner or owners, as a precaution against the excessive debt, or bankruptcy. If after the preventive liquidation an appropriate property liquidation residue remains, the company may not cease in terms of material.

Methods of liquidation of the company can be viewed from various perspectives:



- ***According to the impact on business:***

- **Formal liquidation**, in which the company ceases only legally, but its business activity continues. It is the change of a legal form of enterprise or the fusion.
- **Material liquidation** in which the business activity stops and the company generally as well as legally ceases.

- ***According to the extent of liquidation:***

- **Partial liquidation** of the company, which is only part of the total monetization of complex corporate assets. From the liquidation funds obtained the company liabilities are paid, or part of the company's capital returns to the owners.
- **Complete material liquidation** of the company, which includes its legal liquidation. It comes to the termination of the business and monetization of all assets, while the funds are used to pay the liabilities and the residue is divided among the owners.

- ***According to the impulse for liquidation:***

- **Voluntary liquidation**, which may have various reasons, which differ according to the intended extent of liquidation and, depending on the legal form of the company:
  - free choice of business owners,
  - owner's death,
  - withdrawal of the shareholder or shareholders with a controlling share capital,
  - denunciation of loans by the creditors,
  - expiration of time period or fulfillment of the purpose for which the company is set up,
  - decision of qualified majority of shareholders at a general meeting,
  - effort to avoid bankruptcy or judicial restructuring.
- **Forced liquidation**, which may be caused by:
  - inability to pay back the loan, which was covered by mortgages on certain real estates of the company, or the creditor granted the lien on the part of the movable assets,
  - failure to fulfill obligations to its creditors and offer to settle the liabilities partially in the form of settlement,
  - result of bankruptcy.

#### **4.6 Utilization of crisis**

Activities for the crisis management in the enterprise does not end, since every crisis is an experience associated with information on how to:

- remove the crisis outbreaks, or how to blunt their blades,
- prevent future crisis,
- behave in a crisis in the future.

After solving the crisis, it is appropriate to convene the crisis team members who have participated in managing the crisis and assess the lessons learned from the solution of the crisis phenomenon. If consultation is conceived as the activities to develop the company reputation for blunting the effects of future crises, then the public should be invited to the meeting as well.

After mastering the crisis, it necessary to answer the following questions:

- How can the known deficiencies of the company be removed?
- How can we achieve that the trouble areas and processes in the company run smoothly in the future?
- How can we use experience and knowledge gained from the removal of the crisis to cope with future crises?

Based on the answers the measures are formulated, by which it is necessary to determine their feasibility in the enterprise. The necessity to use the findings of the solution to the crisis represents a continuous process.

The assessment of achieved results must be carried out within the control activities on a regular basis, according to a predetermined timetable, focusing on:

- regular inspections of the crisis management plan,
- reviews of training and emergency preparedness of crisis teams,
- reviews of the training programmes with a focus on risks prevention,
- assessing the readiness to carry out periodic audits to enable the assessment of crisis management,
- periodic reviews of documentation,
- verification of the crisis management effectiveness, its comparison with other companies in order to gain knowledge and experience,
- continuous improvement of communication of senior, middle and executive management for improving the crisis management system of the company.

The integral part of the crisis management phase is represented by recovery stage, which is usually associated with the ability of the company to respond to the interrupted functionality by implementing a corrective action plan to restore critical business processes and activities. The recovery from the crisis not only involves the formulation of plans for possible future types of disasters that can paralyze the functioning of business processes, but also activation measures while allowing avoiding such disasters.

## 5 RESTRUCTURING

Extent of restructuring benefits in Slovakia depends not only on the form of the ownership structure, but also on the structure of the logistic control of a business activity and in particular on the availability and cost of the funds determined for business. Not all the subjects involved in the ownership of enterprises have the potential to start a deep restructuring. Frequent lack of the access to finances, market, expertise and also often to the internal management structure.

Restructuring projects in the Slovak companies are apparently under strong social pressure and the phenomenon of employment. Many of the businesses still suffer from the lack of capital, unsuitable enterprise deployment and lack of management skills, which reflect the new, more demanding criteria of the European and world markets. There is a need to enhance the ability of managers in the preparation of strategic plans, determining the market potential of products in terms of costs and sales, as well as more operational production planning and logistics. This is carried out in the course of preparing the businesses for potential capital investors, in convergence of accounting practices to the European standards, as well as in the adaptation of management structures to new business conditions.

Sustainable economic development and low inflation require the corporate restructuring, financial settlement of companies, termination of non-vital companies and entry of new subjects to the economic scene.

The restructuring is an important attribute of the transformation of the corporate sector. In the broadest sense, it includes policies and economic processes that enhance the performance of the economy as a whole and within particular business sector. In a closer sense, the restructuring of the corporate sector adapts to the new conditions in all directions, such as to the change of ownership, size structure and sectoral composition.

Synek [150] defines the **restructuring** as a change in the structure of a particular organism. The restructuring can be implemented on the structure level of the individual branches of the economic sphere or via the changes in production or business activities.

The European Parliament defines the *restructuring as one of the special forms of industrial transformation. Typically, it is a sudden and often forced adaptation to the new company claim in the economic context, in order to regain the competitiveness.*

Depending on the extent of restructuring changes we can distinguish:

- **Macroeconomic restructuring**, which represents the change in the structure of each sector of the economy.
- **Microeconomic restructuring**, in which there is a change in the company structure. Restructuring may take various forms. It may be:
  - **voluntary and controlled process** that is consciously controlled by the owners and managers of enterprises,
  - **compulsorily controlled process** that is caused by a state of the enterprise, and is modified:
    - in general legislation (Commercial Code),

- in special legislation (Act on Bankruptcy and Restructuring).

In the restructuring it is necessary to leave the well-established business practice of partial solutions and focus on complex solutions based on corporate management. The issue of restructuring is primarily a matter of the authorities' decision regarding its implementation and is also closely linked to the effectiveness of the business activity of economic entities in the economic environment given.

## **5.1 Macroeconomic restructuring**

Complete picture of the future structural changes in the economy requires the definition of the following:

- **role of state** in their implementation,
- **role of corporate sector** in this process.

For the formation of the parametric environment for the business community orientation in their own business it is necessary to process the set of system measures based on the action of financial and economic tools. The role of government in the process of business restructuring is associated with the establishment of an appropriate legislative framework for some important issues, which mainly include:

- definition of the position of minority shareholders, in terms of increasing complexity of processes of the ownership assertion,
- analysis of legislative changes related to some segments of corporate administration,
- mergers, acquisitions, involuntary takeovers and defense mechanisms against them.

According to the form of action, the system measures focused on supporting the restructuring of the economy can be divided into two groups:

- **Measures that are active** in term of the behavior of economic subjects. That is, they support the activities focused on structural changes.
- **Measures that prevent the emergence or persistence of negative effects.** These measures are more punitive in nature. They complement the first group of measures.

The aim of using two groups of measures is to build an environment for the proper functioning of the market. The following measures should be avoided:

- significant help nonviable sectors and firms,
- establishment of mechanisms that distort the market and competition,
- provision of volume and open-ended subsidies,
- writing-off the debts, without corresponding obligations in relation to the restructuring of the production.

Appropriate measures and state initiatives are as follows:

- developing of small and medium enterprises,

- promoting employment,
- training and retraining,
- improving infrastructure,
- supporting research, development and quality,
- supporting the development of infrastructure and information system.

Economic systems of each country are based on a number of **cultural, historical, social and economic differences**. This has also led to specific models of restructuring, and corporate management. Historically, two basic models of corporate management have developed:

- **external model,**
- **internal model.**

In the past, there existed significant differences between these models, but in the context of internationalization and globalization of business it came to the interconnection of some characters as well as to a specific convergence. According to the results of international research organizations, in practice, it is now possible to distinguish *four basic models of business restructuring* and existing systems of corporate management:

- **English** used by 18 countries,
- **German** used by 6 countries,
- **French** used by 21 countries,
- **Scandinavian** used by 4 countries.

Various restructuring schemes differ by three basic characteristics:

- rights of creditors,
- rights of shareholders,
- enforceability of the law.

It is difficult to precisely assess the viability of each model. Each model has some advantages and disadvantages. One system strengthens the mechanisms to facilitate the position of creditors, the other tries to give preferences to the shareholders in their efforts to vote and leave the company, when the enterprise management does not behave accordingly.

Choosing the right model of restructuring is affected number of factors:

- geopolitical differences,
- achieved level and level of economic development,
- structure and state of banking,
- national legislation,
- social security systems,

- different position of the enterprises' relationship and banks in economies,
- willingness of people to invest their funds in securities.

### **5.1.1 Regulation of restructuring from the point of view of OECD**

The OECD is one of the institutions, which is currently developing a programme dedicated to corporate restructuring and administration. It presents a set of regulations, which companies should voluntarily follow. The regulations are based on the assumption that there is no single model that is clearly appropriate for the administration and corporate management. OECD principles, therefore, are not binding and do not provide detailed instructions for the national legislation of the Member States of the organization. They are assumed to be evolutionary in nature, i.e., they they should be developed and used with respect to the overall design of the businesses operation support. The framework of corporate management should protect the fundamental rights of shareholders, which include the rights to:

- secure methods of ownership registration,
- possibility of transferability of shares,
- obtain relevant information about the company in a timely manner, regularly and truthfully,
- ensure participation and voting at the General Meeting,
- possibility of electing the members of the statutory bodies,
- possibility of deciding on the proportion of the company profits.

OECD bodies should assist governments in their efforts to evaluate and improve the legal, institutional and regulatory framework for corporate management and provide guidelines and recommendations to stock exchanges, investors, corporations and other interested parties, which play a crucial role in the development of corporate management. Principles focus on publicly traded companies.

OECD efforts to present a role model stems from the knowledge that the administration, management and restructuring are the key elements of continuous improvement of economic efficiency.

### **5.1.2 Regulation of restructuring by the European Union**

The approaches to existing and future structures and integrated national economies change qualitatively. Due to the globalization it comes to clustering and forming of large international groups, and therefore, the European Union efforts to support the enterprises not only on the national levels, but on the European level as well.

The European Union, as the initiator of the international market opening, provides the necessary funds to support the restructuring and its social and environmental consequences. Restructuring shall not constitute a step backwards in the social area and cause economic losses. Public authorities can help ensure that restructuring takes place under normal conditions.

A stable, predictable and **coordinated macroeconomic conditions in Europe** are an important basis for successful managing the restructuring measures. The local conditions in which restructuring take place are crucial and must be part of the policy.

The measures to be taken on the European level have to meet four requirements:

- **Requirement of coherence** of individual policies necessary for the growth and restructuring, which are contained within, do not lead to the extinction of the human capital.
- **Requirement of long term** perspective of individual policies, which must be able to anticipate, and thus provide the space for the reaction of economic and social subjects.
- **Requirement of social partners participation** in individual policies. The enterprise restructuring is associated with very high costs, not only for the workers but also for the local and regional economy. Preservation of social cohesion, which is a distinctive feature of the European social model, requires the introduction of accompanying policies designed to minimize the social costs and promote variable sources related to the jobs and income. The essential role is played by the **sectoral social dialogue and European work councils**.
- **Requirement to consider the geographical coverage**, since mainly on the local level the anticipation of changes is the most effective. Regional policy and cohesion policy of the European Union acts as a catalyst.

The most substantial measures for restructuring the companies include:

- review of the European employment strategy,
- reform of the financial instruments and the establishment of a growth adjustment fund,
- establishment of "Restructuring" Forum, which aims at explaining the best practices and analyzing the local restructuring obstacles in their application,
- enhanced monitoring of sectors that are most exposed to short-term restructuring. Source of information on the anticipation and management of companies restructuring on the European level are as follows:
  - European Foundation for the Improvement of Living and Working Conditions, which is managed by ERM – European Restructuring Monitor.
  - ESF – European Social Fund,
  - ERDF – European Regional Development Fund.

In industrial policy there is an effort to promote the **sectoral approach** that allows identifying the tailor-made approaches to the individual sectors. The part of monitoring should not be represented only by economy sector that are in crisis, but as many sectors important for Europe as possible should be analyzed so that it is possible to response to the change **timely and proactively**.

Retaliatory industry can be divided into traditional and modern. Within the European Union distinguishes three groups of classes:

- **Existing attenuation industry**, which must reduce its activity due to lower sales and increased competition – metallurgy, textiles and shipbuilding.

- **Existing competitive industry**, requiring significant investment to maintain existing growth rate – automotive, aerospace and chemical arts.
- **New industries based** on the latest trends in scientific and technological development.

The European Commission, **as the main reasons for restructuring**, provides:

- development of the single European market and the opening-up of economies to international competition,
- technological innovation,
- development of the regulatory framework,
- changes in consumer demand.

### **5.1.3 Regulation of restructuring in Slovakia**

The Slovak economy is small and significantly open economy. The small internal market requires businesses to succeed and gain positions on foreign markets where they are able to compete and where they can place their production outputs.

The management of enterprises must identify the needs of the world market and properly adapt technological equipment and skills of its staff. The ability of Slovak industry to succeed in mastering these new demanding requirements influences its competitiveness and future success of the whole Slovak economy.

**Structural deformations** are manifested in particular in the:

- overall low performance and efficiency of the economy,
- high demandingness of resources and imports,
- considerable technical and technological backwardness, lack of application of scientific and technological progress in production and low competitiveness of production,
- lack of finalization in the production with high proportion of heavy industry and low evaluation of national skilled labor,
- underestimation of the tertiary sector as a whole as well as its individual components,
- poor infrastructure endowment,
- high degree of load and environmental damage.

Finding solutions for the successful development of the economy must be based on knowledge of the current situation and its possibilities. The Slovak Republic inherited a deformed inappropriate structure of the economy. As a part of one state of (the former CSFR) it played its role in forming and ensuring the economic structure of RVHP and the Warsaw Pact. Due to its geopolitical position as well as due to its intellectual and technical levels it has been forced to production, mainly to heavy engineering. Further mainly the manufacture in wood, pulp and paper, glass and food industries was developed, and also the production of building materials, which used own raw material resources.



The transformation of the economy has had a negative impact on the Slovak industry. In comparison with other countries of the region Slovakia is characterized by the lowest rates of participation in international capital flows, especially by the lowest foreign direct investments.

Structural policy in the first stage of the transformation process worked reactively. It was oriented to address the social impacts of transformation, to help businesses in crisis (debt elimination, addressing solvency), less for the changes of active production programmes of affected businesses, or for the boost of production and gain of new markets for the production of these enterprises. Domestic supply requirements did not satisfy the internal demand, nor in terms of the scope, structure, or quality. The structure of the offer was formed mainly by intermediates and products at a low level of processing and finalization.

From the experience of recent years with the restructuring of enterprises is shown that the transformation and restructuring of the Slovak economy, was subject to four basic strategies:

- ***Strategy of illegal tunneling*** in which the new owners paid mostly just the first installment of an undertaking. The enterprise was siphoned off via shifting the income and credits, which were guaranteed by the property of the related privatized enterprise. Slow legal system and state inefficiency in the company recovery has often lasted for years.
- ***Strategy of selling the business to an outside investor***, mostly foreign, who usually operates in the same area. The price that investors pay was generally higher than the price originally paid to the state.
- ***Strategy of restructuring***, which aims at investing in the company and leads it to prosperity.
- ***Strategy of the company as any other company*** in which the owners essentially run the business without restructuring, divestiture or tunneling and besides the payment for the company to the National Property Fund, no further steps are made. The enterprises' value over the next decade decreased significantly as a result of a declining competitiveness.

The emergence of strategies was largely determined by:

- Existing legal and institutional environment, which was characterized by favoring the enterprise managers and family members. The consequence is that breaking the law in order to obtain a personal benefit constitutes for the managers any psychological barrier.
- Uncertain economic, political, legal and international conditions characteristic for the post-communist business environment.
- Unbalanced post-communist environment, which formed the presumption of reduced probability of detection and proving the tunneling, which was also supported by the high number of privatized enterprises in a short period of time and lack of experience.
- Frequent absence of interest of outside investors.
- Unavailability of funds for restructuring the companies by their owners.
- Non-corresponding internal control of enterprises, which also stemmed from unethical state bureaucracy, due to which the activity of management of enterprises is consequently not subject to any control.

- Technological backwardness and lack of development of privatized enterprises that require high investments from the owners.
- Option to use available human resources and market potential.
- Clear property in terms that a particular person or group controls the majority of shares.
- Selling price of privatized enterprises, which was significantly lower than the value of their assets. In the Slovak privatization, the enterprises selling price was determined in average to 25 % of the book value of business assets. The first installment, which often represented the only payment for the enterprise was set at 10 % of the selling price, which represented 2.5 % of the book value of the company assets.
- Intangible assets of the business, which was not included in the selling price of the company and has often a significantly higher value than the tangible company assets. Intangible assets, such as the market position, brand and staff were attractive to the outside investors and business restructuring.
- Aversion of the owners to risk, which was caused by an insufficient amount of their property. As a result, the value of enterprise shares they own, usually exceeds their other assets, ten times, hundred times, and sometimes a thousand times. In average their aversion to risk was high, mainly if the shares represented their only opportunity to gain real wealth.

A pressure was developed on Slovak businesses owners and forced them to form and accept the elements of modern competitive management comparable with western market economies. In the process of restructuring of the Slovak enterprises, first it is necessary to exclude unproductive activities and eliminate the excess in the production factors, which also applies to labour and which is one of the greatest challenges of the transformation of the transitive economies in the socio-political sphere.

The enterprises need to develop and internally integrate new departments such as management accounting, finance, marketing, human resource management and determine how these activities in the business management should behave.

The cardinal issue is to increase the pressure on compliance with financial obligations. The balance in the economic relations, which are deformed by insolvency can be maintained only by fully applying the principles of bankruptcy and judicial restructuring. In the past, the schedule proceedings, sell-off the assets and liquidation of enterprises were applied. The new procedure is to preserve the productive functional centres of the enterprise and jobs.

## **5.2 Restructuring of enterprises**

Within the micro-economic restructuring, there are changes in the company as a whole or on the level of its individual parts. The restructuring means total reorganizing of the company and recovery of all of its business activities.

The restructuring is represented by business-oriented and systemically integral (holistic) changes in the management structure of the controlled organizational unit – the company, business, autonomous business units and the like. It is the process of overall changes in the enterprise, based on the implementation of appropriate restructuring measures. They are broad and strategic changes that dramatically affect the future activities of the company.

**Enterprise restructuring** is based on the changes that affect all areas of business life. Restructuring represents a principle *remodeling of business strategies, structures and processes and their alignment with the new reality of living*. It relates to the modification of manufacturing, enterprise resources, their interdependence and their use and may be also associated with the changes in the organizational architecture. It is a process of source protection, innovative changes in the design and mutual harmonization of the structures of the production programme, production and technological, functional and organizational structures, personnel structures and other special-purpose structures, in order to ensure the efficient and effective functioning of the reproductive process.

Sometimes the term enterprise restructuring refers only to the changes in assets and company capital structure or in its strictest sense, it is only the change of ownership relations of the enterprise.

Revitalization, recovery and turnaround are closely related to the concept of restructuring. They differ in time and scope [73]:

- **Restructuring** is the largest term applied to a wide range of profit and non-profit enterprises in a wide range of activities, including financial restructuring, restructuring of business processes and restructuring of operation.
- **Revitalization** includes long-term investments in plant and equipment, staff training and start-up of new businesses, but generally focuses on companies whose performance is declining. There are changes in the existing parameters of the corporation, strategies, structures, corporate culture, in order to catalyze the evolution which leads to the re-invigorated factors affecting the healthy development and prosperity of the company.
- The process of **recovery** is an intervention to identify the operational causes of financial problems in the enterprises and stimulate the management to remedy these operational problems by a fast and decisive action. It aims at improving the cash flow, which can be achieved by changing the cost structure, capital structure, improving the use of business assets, or making the operational changes that increase the business efficiency and performance. The recovery is a process primarily focused on addressing the immediate causes of the negative cash flow. It deals with the analysis of company operation economy, dynamics of cash flow, strategic position and use of the knowledge when deciding on corporate restructuring. In terms of time the recovery as a specific form of restructuring is an intensive short-term intervention.
- **Turnaround** strategy represents a radical renewal of the business ability to act, fast transition to the company healthy basis, overall line of restoring the competitive position of the company, recovery, rehabilitation and reconstruction.

### **5.2.1 Nature and reasons for corporate restructuring**

Restructuring measures may be implemented at each stage of the business life cycle, beginning from its inception, through growth, stabilization, crisis and the collapse. The restructuring is a necessary and sometimes existential phenomenon in the life cycle of a business. It is implemented because of the need to ensure further development of the enterprise, in order to ensure the future existence of the company.

In addition to the traditional understanding of the relationship of corporate crisis and restructuring it should be emphasized that the restructuring may not be associated only with

the crisis in the company. **The restructuring processes can be carried out even in companies that have no problems**, but respond to the changing conditions and strive to constantly improve their competitiveness. *Ideally, the restructuring is implemented as a precautionary measure, and the company receives a competitive advantage.*

To begin the process of restructuring the enterprise may face a number of reasons, which can be divided into four groups:

- **crisis** requiring a radical solution because it threatens the prosperity, stability and future existence of the company,
- **issues** that are less urgent and stressful situations and conditions that arise in the course of the company existence and could lead to the situation such as crisis,
- **prevention**, which represents the company's efforts to prevent potential problems in the future,
- **opportunities** that allow getting ahead the competition and consolidate the leading position on the market.

The reason due to which the company carries out certain restructuring measures, determines the nature of the restructuring process and applied restructuring measures. Depending on this there are (Figure 5.1):

- **Strategic restructuring** that lies in the implementation of strategic interventions and long term measures. The strategic measures are associated with the development stage of the company life cycle, and the companies use them as a precautionary measure and utilization of opportunities. They are also useful in the crisis management when strategic actions follow the operational measures.
- **Operational restructuring**, which is based on the implementation of operational, short-term interventions and measures. Operational restructuring measures are implemented in order to solve the crisis or problem situations and conditions. For this type of restructuring, the term *corporate revitalization* is used.

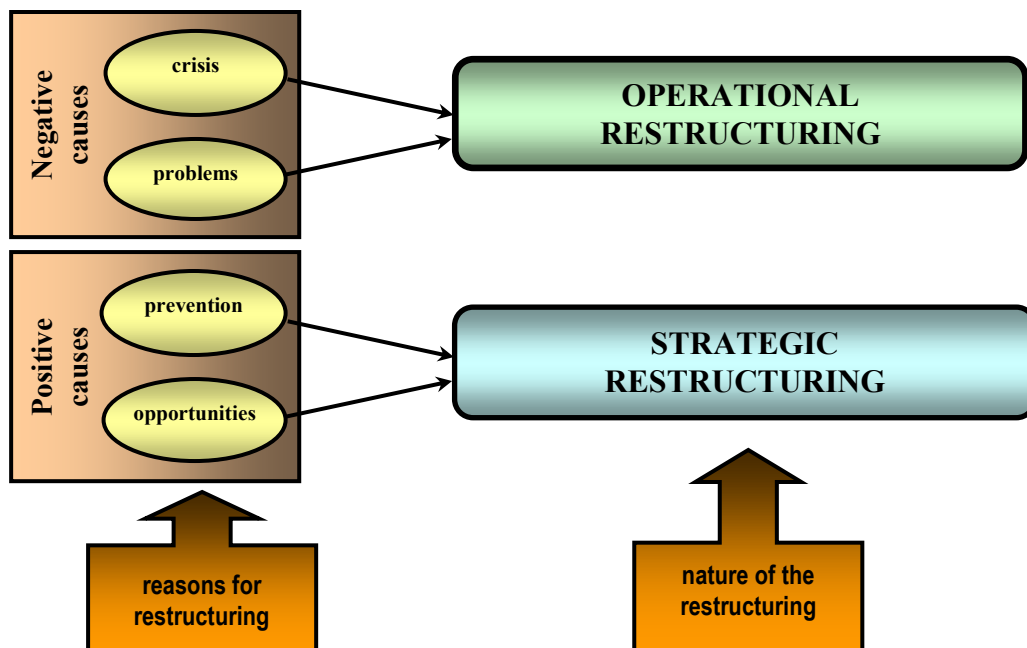


Fig. 5.1 Operational and strategic restructuring

Restructuring is usually understood as a solution to the crisis situation in the company. The reason for the company restructuring may be a long-term decline, which may be caused by:

- changes in the functioning of the market,
- changes in technology,
- incorrect management of enterprise,
- need for a high level of revenues to cover the costs,
- low productivity of labour.

The common signal of an impending crisis in the company include a lack of material resources and energy needed to fulfill the orders, a decrease in business innovation, increase of errors, increase of dead-times, decreased productivity at work, stagnation, reduction or fluctuations in sales, growth in the number of customer complaints to service and goods quality, price decline, reduction of the number of customers, worsening business climate, jamming cooperation among company undertaking, decrease of staff training, fluctuation growth, costs growth, impaired solvency, requirements to pay the suppliers in advance or in cash.

**Restructuring** is suitable for businesses that are indebted, insolvent or in loss, whose yield capability can be significantly improved and sustained by the changes in the structure, strategy or costs. It is a process that is largely affected by the quality and consistency of its strategy implementation. Restructuring is the process of overall changes in the company, which is based on the implementation of appropriate restructuring measures. It has an impact on employees, suppliers, customers, debtors and creditors.

Restructuring is usually implemented as a remedy. It uses the tools and techniques are cross-functional in nature. The process starts at the time of the first signs of crisis or in the process of the acute crisis. It stands that the sooner the restructuring is implemented, the lower the costs associated with saving are.

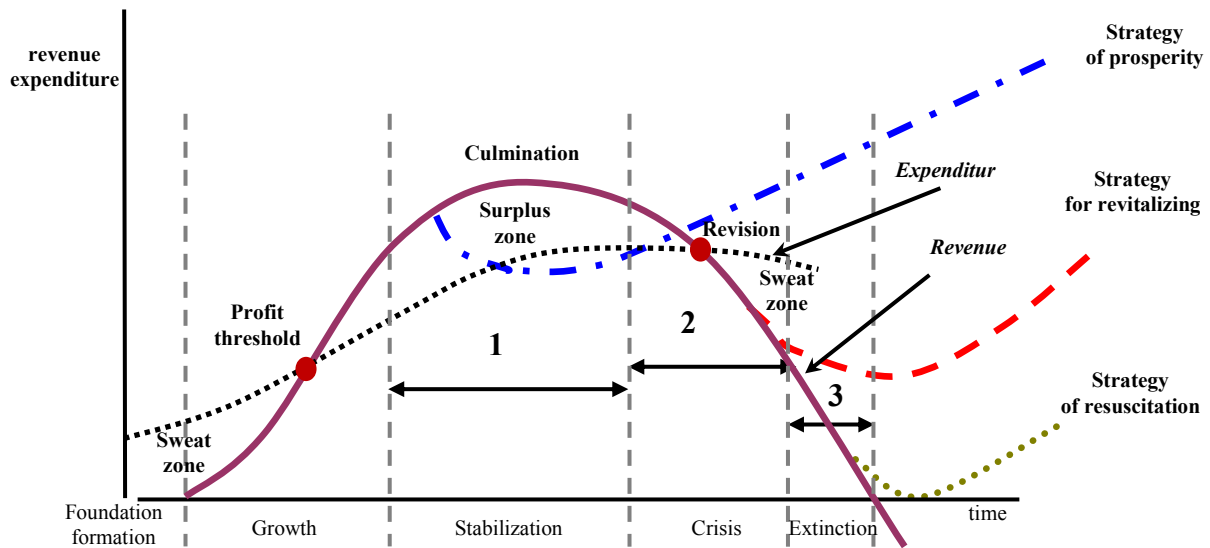
### **5.2.2 Restructuring strategy**

The distinctive feature and the key moment of this emerging company recovery process is represented by the moment of its beginning. The important thing is to recognize the status of the undertaking at the time when the healing process starts. At the moment of the beginning of this long and complex innovation company process, there is a thought-out and prepared termination of the existing business activities. Immediately afterwards, in the form of turnover, there is an immediate initiation of large-scale changes that give rise to a new business.

Depending on the stage of the business life cycle, in which the enterprise at the time of commencement of the restructuring is, it is possible to examine the restructuring strategy. From this perspective, there are three possible restructuring strategies as shown in Figure 5.2, which condition the further development of the company:

- **prosperity – quantitative recovery,**
- **revitalization,**
- **resuscitation.**

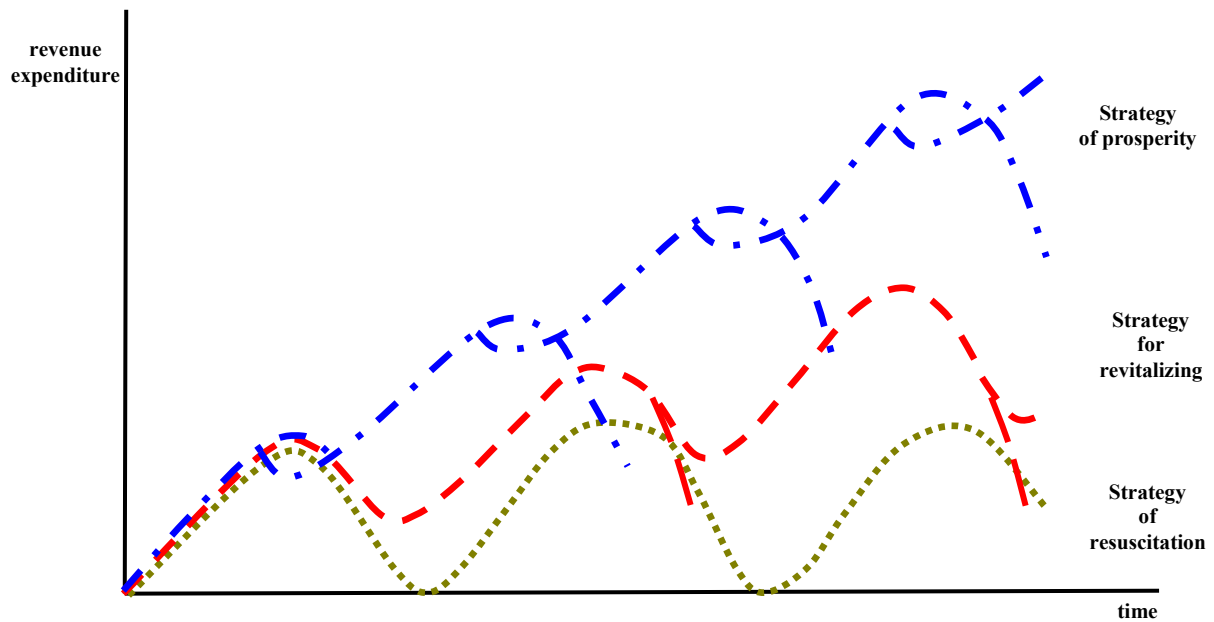
Application of any of these three strategies is conditioned by the stage of the life-cycle, in which the enterprise is at the moment of deciding to carry out the restructuring.



**Fig. 5.2** Restructuring strategies in different stages of the business life-cycle [174]

Corporate restructuring strategies are aimed at increasing the efficiency of the company, or at rescuing the company from extinction. Each strategy is associated with a temporary decrease in performance and prosperity of the company. The overall success of the restructuring strategy depends on the human factor, because it represents an increased burden for the management and all employees. All restructuring strategies are very costly, and only during the strategy of prosperity it is possible to partially use own financial resources.

Long-term viability of the company represents the **process of discontinuity** in the company development. The restructuring allows the company transition from one life-cycle to the other one and then to the next one (Figure 5.3).



**Fig. 5.3** Strategy of enterprise restructuring in the process company discontinuity development [174]

The life-cycle of the company due to the influences and circumstances may not preserve the stages of the life-cycle model. The individual stages are specific, have varying duration, which influences the formulation of strategies applied in the planned restructuring. The restructuring disrupts the continuous course of the company development, which according to the life-cycle, after shorter or longer periods of time leads to the demise of the company. The discontinuity in the company development is the tool ensuring an extension of the business life-cycle.

#### **5.2.2.1 Strategy of prosperity**

Strategy of prosperity applies for the period of business development before reaching the peak period, i.e. the stage of growth and stabilization. It is the most progressive restructuring strategy, which requires the most complex and most difficult decision for its application. The enterprise, opting for the application of the strategy of prosperity thinks about leaving the prior progressive development and about asserting a new and often risky way for further development and company existence. This form of restructuring is applied by the world-class enterprises.

Application of the strategy of prosperity the long-term prosperity can be achieved. It is about the utilization of the favorable effect of waves that still hold the company up, the company achieves great prosperity and efficiency. Each wave should be left at the right moment (Figure 5.3), prior to its full peak, and before this wave pulls the company back. It is the decision to leave the previous positive development of the company and opt for a new journey laden by a considerable risk. Much risk should be compensated by the high probability of achieving even the greater prosperity. Risk decisions can be compensated only by a new, well prepared and greater prosperity, promising business idea or plan based on the competitiveness.

Such a risk decision can be taken only by a high quality, confident and technically competent management team, who bears the strategy, sponsors it and implements the entire radical change.

The success of the strategy depends on the application of the following principles:

- Maintaining the prior owners and senior management, which is competent for the upcoming restructuring.
- Quality business plan based on competitiveness and commercially successful production programme with an extremely high value for the customer, which significantly exceeds the prior business effects production schedule, which changes by the restructuring.
- Facing the high, but calculated risk.
- Quick and understandable decision.
- Centralized management, particularly at the beginning of the restructuring.
- Strict management and direct communication.
- Forming of innovative environment.
- High motivation of all staff to changes.
- Intensifying the work with customers, suppliers and public in order to obtain their support [174].

#### **5.2.2.2 Strategy of revitalization**

Strategy of revitalization is applied in the time of the greatest need of corporate restructuring. The aim of the application of this strategy is to save the company from the decline, bankruptcy and liquidation. The strategy of revitalization is applied at the stage of bankruptcy.

Implementation of the strategy allows radical and total recovery of the company, which shows degenerative signs with all symptoms of a slack business. Declining sales, achieving loss, impaired liquidity, rising debt, negative cash flow, and the like can be considered the characteristic symptoms.

In some cases, due to the lack of preparation of the senior management, there is an interruption of the business activities. The company reduces the costs via unprepared steps that cause a decreasing confidence of customers and suppliers to the company. The enterprise is forced to temporary and later permanent cessation of production and reduction of staff. The work moral worsens, the hopelessness escalates and there is a total collapse of the company.

In implementing the strategy of revitalization it is necessary to apply the following principles:

- Exchange of senior management partially or wholly to blame for the situation.
- Quality business plan must be competitive, with a commercially successful production programme and high added value for the customer.
- Radical and conceptual management of costs optimization.
- Centralization of management and precise control.
- Quick and understandable decisions.
- Radical measures designed to improve the financial situation. It comes to the recovery of claims, rational divestiture of unneeded assets and the like.
- Suspension of investment activity.



- Review of research and development to streamline the product and technological innovations.
- Rationalization of production and work in the company.
- Developing and strengthening the innovation environment.
- High motivation of all personnel to the changes.
- Intensifying the work with customers, suppliers and public in order to gain more support.

The successful strategy of revitalization is capable to ensure the profitability growth of the enterprise, however, to a lesser extent than the strategy for prosperity [174].

#### **5.2.2.3 Strategy of resuscitation**

Strategy of resuscitation is applied at the stage of demise (Figure 5.2). It has to save the enterprise from the complete extinction, which is associated with its liquidation. The strategy of resuscitation allows the company to begin a new stage, which is a continuation of the production, market or employment activity of the original company.

The strategy of resuscitation requires the compliance with the following principles:

- Appointment of an entirely new senior management.
- Quality business plan based on competitiveness and commercially successful production programme of high value for the customer, which continues in terms of the product or technology to the production programme and the production of bankrupt company.
- Centralization of management, particularly at the stage of formation and development of the company.
- Thoughtful, quick and clear decisions.
- Constant care of economical use of company resources.
- Developing and strengthening the innovation environment.
- High motivation of all personnel to the changes.
- Intensifying the work with customers, suppliers and the public in order to gain the trust and support of the company surroundings.

The strategy of resuscitation is capable to generate only a degree of prosperity, which corresponds to its level of prosperity attained in the stabilization stage of the company life-cycle. In practice, it is assumed that after restructuring based on the strategy of resuscitation different variables of the restructuring strategy follow with the properties the prosperity strategy and revitalization strategy [174].

#### **5.2.3 Extent of corporate restructuring**

Depending on the scope of the restructuring carried out in the company we distinguish three levels of restructuring:

- **Operational restructuring** takes place on the level of the enterprise business units. It analyzes the current competitive position of each business unit and its position in terms of

environment protection. It is about finding and identifying the key success factors and the most important factors in forming the value for customers. The cause of the crisis is usually represented by the fact that the business unit is not able to profile in relation to the competition and differ from the competition by some competitive advantage.

Part of operational restructuring strategy is to analyze the various areas of business activities. For each area strategic plan that is built on the financial goals and corporate strategy important points, should be developed.

- **Restructuring of portfolio** based on knowledge of the extent to which the company headquarters contributes to synergistic effects taking place in the enterprise. The headquarters can increase or destroy the total value generated.

The starting points for the restructuring on the level of the entire company are:

- selection and reciprocal links of business activities,
- formation of reciprocal links among the different parts of the enterprise,
- development and building of key competences on the level of the enterprise.

Business units may be divided, merged, or sold. It is possible to consider the inter-departmental transfer of knowledge and experience. The important thing is to decide on the size and scope of the business activities portfolio, notwithstanding the fact that a large diversification shares the responsibility for many corporate crises. In the restructuring of the portfolio it comes to the concentration per small number of business fields and cleaning of the business activities portfolio.

- **Financial restructuring** seeks to optimize the financial and ownership structures. Companies with a high share of equity tend to waste the financial resources, and on the other contrary, companies with a high share of foreign capital paying regular interest, are unable to concentrate and make effective use of financial resources. Financial restructuring must be accompanied with efficient controlling. The central quantity, which is in the process of financial restructuring monitored, is represented by the liquidity.

#### **5.2.4 Stages of development of the view of company restructuring**

As a result of growing intensity of the economic activity, the importance of rehabilitation and restructuring of enterprises increases as well. Before World War I decline in the company was a considered a phenomenon that can happen only to a stupid and reckless enterprise. Due to the adverse external circumstances, such as the oil crisis in 1973, it is concluded that the bankruptcy should be paid a serious attention.

The globalization process causes growth of technological, commercial and legal demands of business. The company management is appointed with even increasing demands. In the context of this development, the importance of restructuring processes grows.

In terms of long-term statistical data, theoretically taken, each enterprise sooner or later is involved in the crisis. It is therefore necessary to have the evaluation method for the company vitality and have a methodology to avoid bankruptcy prepared. In case of an

unfavorable situation in the company, it is necessary to know the methods of restoration of the declining business viability.

The development methodology of corporate restructuring has undergone several development stages. Originally, the restructuring was regarded as something unworthy. Only recently the opinion has been accepted that company remediation is actually involved in the business risk and does not present the shame for the enterprise.

In the first stage of development of restructuring methodology, the attention was paid only to finances. Other aspects of the business have been paid only little attention.

In the second stage of the development, it was all about improving the ratio of the production effort with its results. Using the theory and practice of the workflows according to Taylor and Gilberth operational efficiency was increased and the work tasks simplified. The attention was paid to the time and labour costs, since the share of work was for the price of goods and services, before the introduction of mechanization and automation, the most important item.

Gradually, due to the rationalization of work and partial mechanization, the importance of the work, the price of products and services decreased. Therefore, the focus transferred from improving the overall performance to the study of indirect labour costs at a later stage of methodology development.

The third stage was about the increase of the business performance focused on the amalgamation of unsuccessful companies with successful ones. It is based on the idea that the increase in the turnover of the company the direct costs are proportionately increased, but the revenue growth does not have a corresponding effect on the increase of the indirect costs. The advantage of companies amalgamation with similar production programme and the market is based precisely on this knowledge. For example, to double the turnover, it is only required to increase the indirect costs for general administration slightly.

In the next stage of development, the restructuring efforts concentrated on the characteristics and motivation of employees, especially managers and responsible personnel. This was based on the fact that a trained and motivated employee is the most important factor in a successful business and an essential factor in companies that are less successful.

Currently, there is a prevailing tendency to divide the large business units. Large enterprises originated via an organic growth or amalgamation often become cumbersome in decision-making and their leadership is not enough entrepreneurial in nature. The principle of restructuring consists of dividing the company into smaller business units, in which there is shorter feedback, market adjustment quick and immediate identification of business management with business objectives.

At the same time the market of services specialists and consultants in the restructuring and liquidation of enterprises develops. Consultants are independent, have the necessary experience and assume the defined role for a certain period. In the restructuring there is the requirement that the adviser is willing and able to carry out the task by him/herself and take responsibility for its fulfillment.

Extent of restructuring benefits in Slovakia depends not only on the form of the ownership structure, but also on the structure of the logistic control of the company activity,

and in particular on the availability and costs of financial resources for business. Not all actors involved in the ownership of enterprises have the potential to start the deep restructuring. Frequently, the access to finance, market expertise and often the internal management structure are missing.

Restructuring projects in the Slovak companies are apparently under strong social pressure and the phenomenon of employment. Many of the companies still suffer from the lack of capital, unsuitable enterprise deployment and lack of management skills, which should reflect the new, more demanding criteria of the European and world markets. There is a need to enhance the ability of managers in the preparation of strategic plans, determining market potential of products in terms of costs and sales, more operational production planning and logistics. It is carried out under conditions of preparing the businesses for potential capital investors, approaching the accounting approaches to the European standards, as well as adapting the management structures to global business conditions.

## **6 RESTRUCTURING METHODOLOGY OF SLOVAK COMPANIES**

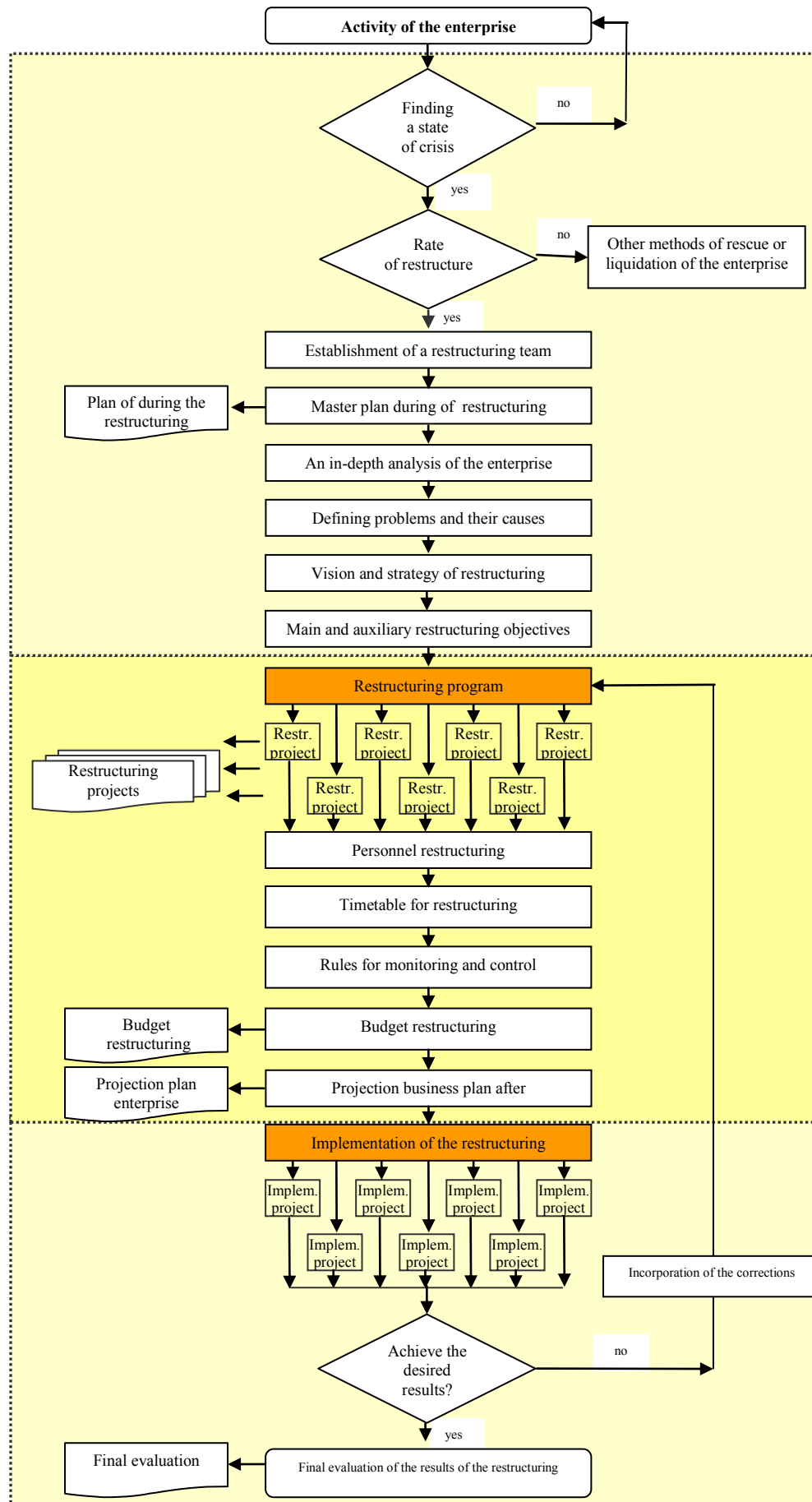
Manage the crisis in the company is one of the most complex management tasks. Master it with the current heterogeneity and complexity of individual circumstances in a particular company, the individual knowledge of strategic and operational causes of the crisis the company is crucial, enabling thus the deployment of effective remedies. Decisions in times of the company crisis are taken under pressure and without relevant information, despite of their strategic importance to the company. Each corporate crisis is also a crisis of confidence and requires the management to give the maximum personal commitment, integrity, consistency, and quality management. The management is required to have a self-critical and open approach because most crises are the result of errors and not the result of general external influences.

The optimal decision is the matter of knowledge, experience and preparation to possible emergencies. The methodology of corporate restructuring is based on this finding, which forms the starting material for the application of restructuring on the Slovak enterprises.

### **6.1 Model of enterprise restructuring**

It is optimal to execute the company restructuring via the basic steps in the following sequence:

1. Find the crises state of enterprise.
2. Determine the extent of enterprise restructuring of.
3. Build a team responsible for enterprise restructuring.
4. Elaborate a framework plan of restructuring.
5. Elaborate thorough analysis of enterprise.
6. Define problems and their causes responsible for the existing situation.
7. Define the vision and strategy of enterprise restructuring.
8. Define the main and auxiliary objectives of restructuring.
9. Elaborate the restructuring programme:
  - Development of restructuring projects for areas, in which the changes will be implemented with the identification of measures to be taken.
  - Appointing the personnel for restructuring.
  - Establishment of a timetable of the restructuring implementation.
  - Definition of rules of monitoring and control.
  - Preparation of budget of restructuring with the determination of financial effects and restructuring costs.
  - Building the business plan projections after restructuring.
10. Execute the restructuring according to programme.
  - Implementation of restructuring projects.



**Fig. 6.1** Model of enterprise restructuring [68]

- Continuous controlling of tasks and compliance with the timetable of restructuring.
  - Incorporation of corrections to the restructuring programme, if necessary.
11. Prepare the final evaluation of the results of restructuring achieved.

Content of individual corporate restructuring steps is described in the table in detail. To implement the company restructuring we can follow the model shown in Figure 6.1.

## **6.2 Identification of company crisis state and eliciting the rate of the enterprise restructuring**

A healthy company is such a business in which there are no doubts about its future. It is able to finance its operations, meet its obligations and generate sufficient profit, which is used to invest in the company and ultimately ensures the adequate capitalization of shareholders' investments. The recognition of the company crisis condition is not sufficient for successful management of the crisis. It requires the identification of the causes, nature of the crisis and other characteristics that allow predicting its course and possible measures to handle it.

The enterprise, which is unable to meet the criteria, should take appropriate measures to restore the vitality of the enterprise. The company troubles may signal its demise, or at least the threat of demise. All other circumstances that affect the business performance and generate negative signs, only cause periodic fluctuations in the company's performance. It is difficult to recognize when it is only a periodic fluctuation of performance of the company and when the company actually gets into a crisis.

Properties and modeling techniques can be effectively used in the analysis of the crisis in the enterprise, regardless of their tangible essence, their prevention and steering the company out of the crisis. Using the basic model of effective action, it is generally possible to derive the performance of an efficiently operating company  $P(t)$  by the following equation:

$$P(t) = f(*U_C(t), *Z_V(t), *Z_{VL}(t), *U_P(t), *O_P(t), r.) \quad (6.1)$$

where:

- $*U_C(t)$  – vector of processing quality of company objective function and definition of the objectives to be achieved,
- $*Z_V(t)$ , – vector of quality feedback between the subject mater and a performer,
- $*Z_{VL}(t)$  – vector of quality of feedback executor and its scope of activities, such as workers' readiness to perform their duties in the company, their knowledge, set of regulations and standards, quality system planning, time program of efficient action and the like,
- $*U_P(t)$  – vector of possible ways of purposeful action of executor on the subject activity and the quality,
- $*O_P(t)$  – vector of potential impacts on the environment and the executor of subject activity.

It is just a gross and symbolic expression of reality. All the vectors are very dynamic and are a function of time and usually are subject to random "r".

If it is possible to achieve the objectives via different ways, it is desirable to choose only such an action, which is advantageous in some respects. Then, other criteria have to be entered according to which the weight to the method of achieving the objectives and decisions is assigned. In the event of a crisis, the executor must be able to decide on their optimal, purposeful action, which requires higher skills. In this case, the enterprise reaches the maximum performance.

$$P(t)_{\max} = f(*U_C(t), *Z_V(t), *Z_{VL}(t), *U_P(t), *O_P(t), r.)_{Opt} \quad (6.2)$$

Performance of a well-functioning enterprise generally oscillates in the vicinity of the maximum performance of  $P(t)_{\max}$ , but most often on the level of pre-qualified certain nominal value of  $P(t)_{nom}$  according to the type and quality of the enterprise, for example in the range of:

$$P(t)_{nom} = (0,92 \div 0,98) \cdot P(t)_{\max} \quad (6.3)$$

Any properly sized business can work in the short term with higher performance than  $P(t)_{\max}$ . The use of surplus activities can be used for the short-term crisis prevention.

There are limits when a company presents such a low performance that it loses its functionality. The falls below this threshold gets the company into the state of crisis. If the appropriate measures to steer the company out of crisis, then the company sooner or later collapses.

The enterprise crisis can be defined by the decline in its performance below the qualified minimum threshold when the company loses its functionality, by the following equation:

$$K R_{\text{sys}} \langle \min P(t) = f(*U_C(t), *Z_V(t), *Z_{VL}(t), *U_P(t), *O_P(t), r.)_{\min} \quad (6.4)$$

By the decline in performance below the following specified limit the company gets into insolvency [93].

The determination of the extent enterprise restructuring is essential for achieving the corporate restructuring. To obtain the answers it is necessary to examine:

- internal and external factors that may affect the company's ability of restructuring,
- readiness and capacity of current or future company management to implement the restructuring,
- attitude of the company owners to restructuring.

At the beginning of the restructuring it is necessary to determine whether those responsible are willing to accept the changes in the company, and if they are able to execute these changes and identify the individual measures that will lead to the improved business efficiency.



**Tab. 6.1** Questionnaire for establishing the enterprise restructure [68]

<b>I. Perspective owners and top management</b>	
<i>Recovery may require significant changes in the operation, structure of assets, capital structure and staff because those steps needed to restore the company, have a significant impact on the operation, it is absolutely necessary to take into account the perspective of the owners from the beginning of the restructuring process.</i>	
<b>Questions for owners:</b> <ul style="list-style-type: none"> <li>▪ What is the share of the assets and the degree of control?</li> <li>▪ How to invest?</li> <li>▪ Coupons, cash or as a spin-off?</li> <li>▪ Was company purchased for its financial or strategic value?</li> <li>▪ What is their opinion on management?</li> <li>▪ What are their financial goals?</li> <li>▪ They want change?</li> </ul>	<b>Question for general director:</b> <ul style="list-style-type: none"> <li>▪ Technical expertise and market knowledge.</li> <li>▪ Long-term strategy and short term goals.</li> <li>▪ The degree of control and employee relations.</li> <li>▪ What is his assessment of the situation?</li> <li>▪ What is the interest in the recovery business?</li> </ul>
<b>II. Financial perspective</b>	
<i>The basic sources of data for the analysis are:</i> <ul style="list-style-type: none"> <li>▪ financial statements,</li> <li>▪ interview with financial director,</li> <li>▪ management accounting.</li> </ul>	
<b>Financial indicators of crisis:</b> <ul style="list-style-type: none"> <li>▪ Payments: Is the enterprise's ability to pay interest on loans and repayments of principal? The company is able to pay taxes, payroll, accounts payable to suppliers?</li> <li>▪ The firm penalized for late payments?</li> <li>▪ What is the financial condition of major customers?</li> <li>▪ What is the result of the comparison overheads firm and its main competitors?</li> </ul>	
<b>III. The prospect of traffic and quality</b>	
<i>The tour company will reveal many. Poorly maintained venture is a sign of weak enforcement of quality. Activity level workers may indicate inadequate production planning, poor marketing or middle management. On the enterprise should be viewed from above and the needs of recovery.</i>	
<b>IV. The prospect of marketing and sales</b>	
<i>Business evaluation examines the relationship between the company and its customers and suppliers. Regardless of how well the enterprise is organized, and what financial security holders, if the enterprise has no products that customers are willing to buy, recovery is impossible enterprise.</i>	
<b>Marketing questions:</b> <ul style="list-style-type: none"> <li>▪ What is the main occupation?</li> <li>▪ How many variations of products manufactured by the enterprise?</li> <li>▪ Amended enterprise marketing focus?</li> <li>▪ What is the financial situation of the customer?</li> </ul>	<b>Business questions:</b> <ul style="list-style-type: none"> <li>▪ Program: the product's complexity, size and variation.</li> <li>▪ Trends in sales of main products. Were shifts in the core business?</li> <li>▪ Markets and distribution, domestic market, export markets, retail / wholesale.</li> <li>▪ Main competitors. How to stand firm in comparison with them?</li> <li>▪ Main contractors and difficulties in obtaining major suppliers.</li> <li>▪ Competitive advantages (cost, quality, time, mixed, none).</li> </ul>

To determine the extent of the company ability to be restructured it is necessary to perform a quick analysis of the situation in the company. The structure of the questionnaire to determine the extent of the company ability to be restructured company is listed in Table 6.1.

### **6.3 Organizational support of restructuring and its course**

Restructuring team should be composed of internal and external specialists. Restructuring can utilize the services of external consultancy companies experienced in enterprise restructuring.

The internal members of the restructuring team are drawn from specialists from different functional areas of the company, who take over the role in the company associated with the implementation of the restructuring as part of their duties and responsibilities. Mostly they become the part of a matrix organizational structure. The internal part of the restructuring team should be composed of the following associates:

- member of executive management,
- manager of logistics,
- operative from the production,
- operative from the enterprise administration,
- sales engineer,
- operative responsible for the enterprise safety,
- member of the operational board.

The utilization of a specialized consultant who is not directly from the company, since such a person can perceive the differently, without being burdened with troubles, and has the ability to bring new thoughts and ideas, is important.

A member of the restructuring team should possess the following competencies:

- **ability to understand the tasks** for which the critical thinking and strategic foresight are necessary,
- **ability to perform tasks and provide activities and processes**, which require a proactive approach, self-confidence, self-control and flexibility,
- **ability to lead teams** through motivation, interpersonal skills and interest in the business outcomes.

To cope with the task of restructuring it is necessary to have:

- personal prerequisites and ability to handle various pressures in promoting the changes,
- ability to identify a small group of capable professional enthusiasts who are convinced of the correctness of the chosen path and will work closely in a team,
- analyze and separate the real cause of the problem from the indirect and virtual ones,
- actively communicate with internal and external key players,
- not to hesitate and delay the decisions,
- keep checking the implementation of decisions,
- ability to handle the crisis timetable.

For successful restructuring, the head of the restructuring team should have at ***least one successful process of restructuring passed***. It should be a strong personality that handles crises and stress. ***High psychological stress*** during the period of restructuring may cause a reaction of looking for an escape and panic, and as the manager bears full responsibility for overcoming the crisis, s/he must suppress their own efforts to escape and focus on how to cope with this situation as well as require such an approach from their subordinates. In the process of carrying out the tasks of restructuring s/he becomes the only decision authority and their orders shall be followed by all, hence by the other managers whose powers are temporarily restricted.

Head of the restructuring the team has to ***go for his/her vision despite the obstacles***, even when others fall off, because s/he has a dual mission:

- S/he must ensure that their view and views all employees focuses on the essentials, the main objectives of corporate restructuring.
- S/he has the one who gives direction, so that the company does not handle the trivialities, secondary and random troubles.

#### **6.4 Framework plan during the restructuring**

Before the start of the restructuring it is necessary to develop the framework plan of the restructuring course. Its importance lies in the fact that it limits the individual activities and should contribute to the reduction of time for the preparation and implementation of the restructuring and elimination of unnecessary dead-times that may be crucial to the success of the restructuring. Fast and accurate decision-making and action that saves the values in the business is required.

Within the framework plan of the course of the restructuring preparation and implementation it is appropriate to indicate the duration of the actions and responsibilities of the various members of the restructuring team. Mostly it is compiled using the logical framework, or in the form of Gantt chart.

#### **6.5 Deep analysis of the company**

Foundation and prerequisite for business restructuring are represented by properly analyzed initial state of the company and revealed strengths and weaknesses of the company. For the decision making all available and relevant information from internal and external sources are utilized.

Business restructuring should begin by a thorough analysis of its current state. The crisis in the venture would show many internal and external manifestations (Figure 6.2), but it is necessary to specify the state in which it is currently located.

The focus of the initial state analysis is on hard business data, strategies analysis, market and competition. The aim is to quickly identify the causes and factors of the crisis and obtain the necessary data to determine the ways of handling the current crisis. Analysis parts of the initial situation shown in Figure 8.3 are certain calculations, which can be adjusted according to the needs and specifications of the business.

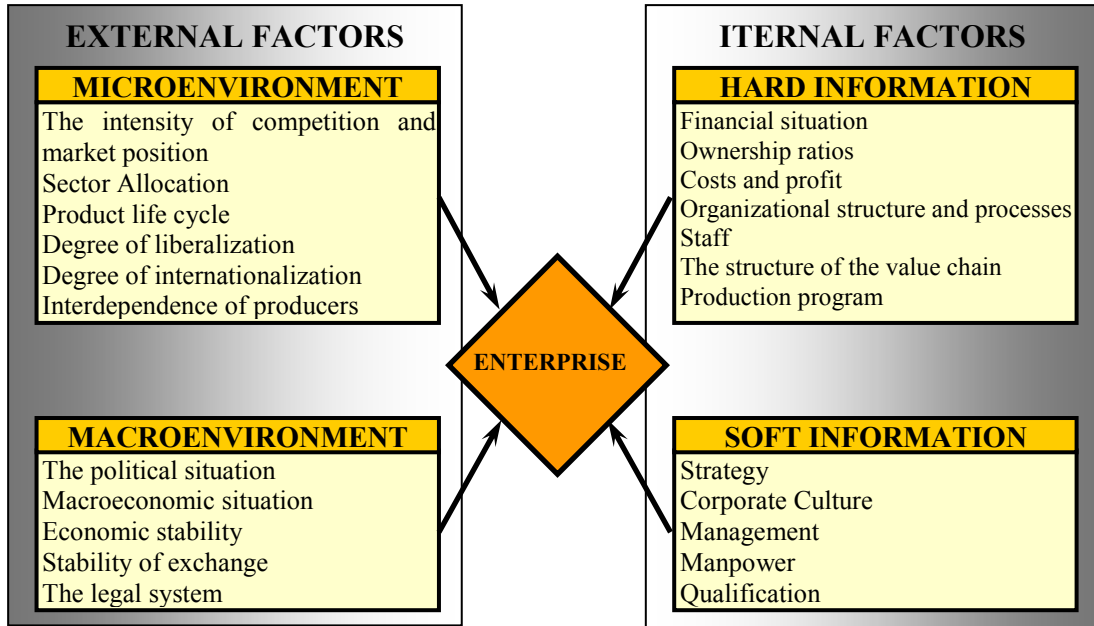


Fig. 6.2 Factors influencing the initial state of the enterprise

To execute a broad restructuring project, it is necessary to carry out a deep analysis, which is an instrument of knowledge of the current state and company development. A deep analysis of the company presents an analysis of economic and non-economic factors from internal and external perspectives. The company analysis comprises the basic information about the company, business, personnel, financial analysis and analysis of production.

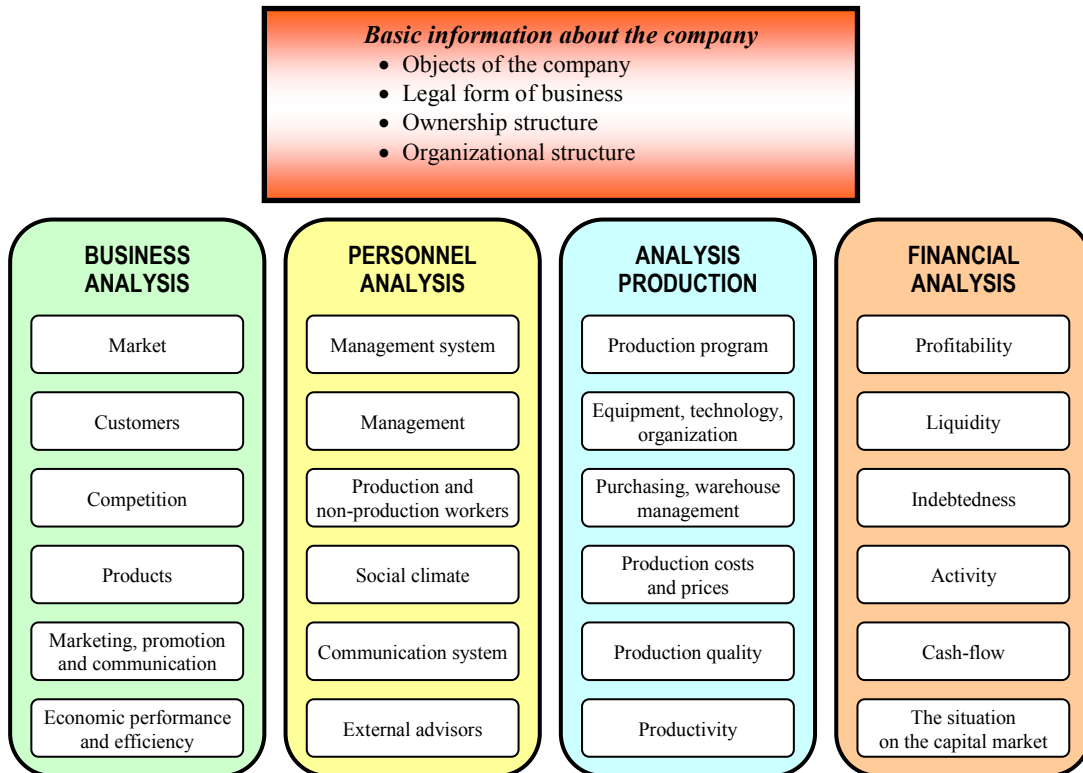


Fig. 6.3 A deep analysis of the company

In the context of the analysis oriented on **basic information about the company** the attention is paid to the primary data of the subject of business, legal form of business, ownership and organisational structure.

For the main internal documentation for the deep analysis, depending on its purpose, can be considered the following: current certificate of incorporation, partnership agreement, articles of association, balance sheet, income statement, cash flow statement, statement of changes in equity, list of tangibles and intangibles, list of stocks of materials and goods, list of assets and liabilities, credit, pledge, lease and rental agreements, information about activities in other companies, a comprehensive management and business plan documentscan.

In some cases, information on macroeconomic development of the country, the development of the market for goods, labor and capital are necessary documents as well. The source of these data are represnetd mainly by websites and publications of various institutions such as the National Bank of Slovakia, Slovak Statistical Office, Bratislava Stock Exchange, ministries, banks and organizations specializing in financial advice.

**I. Business analysis** is focused on the business prospects of the department and its strategic objectives, the position on the market, competitors, products, research and marketing in particular directions. Particular attention is paid to assessing the economic performance and business efficiency.

**Trading position** of the company in the process of restructuring is assessed in terms of:

- *Cost reduction potentials*, which can be achieved by reducing the size of the technical department and integrating the production, quality control section of consolidation and other corporate departments. The company must consider the use of outsourcing for some activities that are ineffective.
- *Responsibilities for achievements* that can be precisely specified and appoint a specific manager that will control their performance. One manager should be responsible for the operation, including manufacturing, engineering and purchasing functions to manage the scheduling of material resources.
- *Functionality business activities*, which is based on the a ccess to markets, defining customers and meeting their needs.

**II. Personnel analysis** is focused on enterprise workers. In the framework of assessing the management system, the balance of knowledge and skills of workers, both at senior management of the company, as well as at lower hierarchical levels is carried out. The social climate is evaluated, the communication and flow of information and cooperation with the external advisors is verified. **Human resources** are evaluated in terms of their number, workload, motivation and results of the work.

**III.** The subject of **analysis of production** focuses on the manufacturing program in relation to the production equipment, technical equipment and technology, the attention is focused on the production schedule, i.e. the assortment composition and volume of production, equipment in use and technology, organization of production, purchasing organization, management of stocks and their valuation, then to the management accounting roles, functions and status as a part of management information system, next on production quality, but also on the individual production factors productivity and overall productivity.

**Production processes**, forming the core of the company value chain are evaluated regarding the following:

- effectiveness of purchasing and invoicing,
- length and the time course of the production cycle,
- quality defects and claims.

**IV. Financial analysis** is focused on the core groups of indicators characterizing the financial position, such as profitability, liquidity, debt, activity, cash flow, and in enterprises whose securities are placed on the capital market, the indicators characterizing the situation on the capital market. The observed values of indicators are compared to a certain basis that is determined in terms of time, space, plan or determined on the basis of expert experience such as standard.

The financial analysis comprises the analyses of:

- *Segmentation product ranges and contribution margins*, which is based on the segmentation of the company assortment into different categories. The product range can be segmented by the type of the product, markets and customers, size, origin of manufacture of the product, types of products or prices. The defined product segments are compared from a financial point of view, analyzing the direct costs of the segment and calculating the contribution margin of each segment.
- *Fixed costs* represent a significant part of the total costs of the company and are a source for costs reduction.
- *Cash flow*, which is assessed in terms of income and expenditure, both from structural and time perspectives.

The deep analysis output is to identify the main troubles within the company as well as the causes that cause them. The interdependencies of individual problems and their impact on the financial management of the company are identified. Conclusions of the deep analysis of the company are the basis for next steps in the process of company restructuring.

## **6.6 Strategy, vision and goals of corporate restructuring**

After the evaluation analysis of the initial state it is needed to formulate a new strategy for the enterprise to which the company wants to revise restructuring as quickly as possible. The new strategy should reflect position in the company and its environment at maximum. Experience has shown that it is appropriate to process the strategy according to the project management principles. For the quite short period of time of corporate restructuring, the strategic and operational projects that are taking place in parallel, even if they have different objectives are used.

- **Operational projects** are aimed at reversing the unfavorable state of the company and have a direct impact on the financial statements of the company. They focus on financial indicators, such as reducing costs, freeing the funds.
- **Strategic projects** are designed to improve the competitive position of the company. They should lead to a fundamental change in the corporate structure. They aim at:

- analysis of the production structure in order to lean the production programme,
- use of outsourcing,
- account of the development of new products,
- assessment of logistics concepts and fundamental reorganization of the company.

The basis for the restructuring programme development should be to define the corporate restructuring objectives to be achieved.

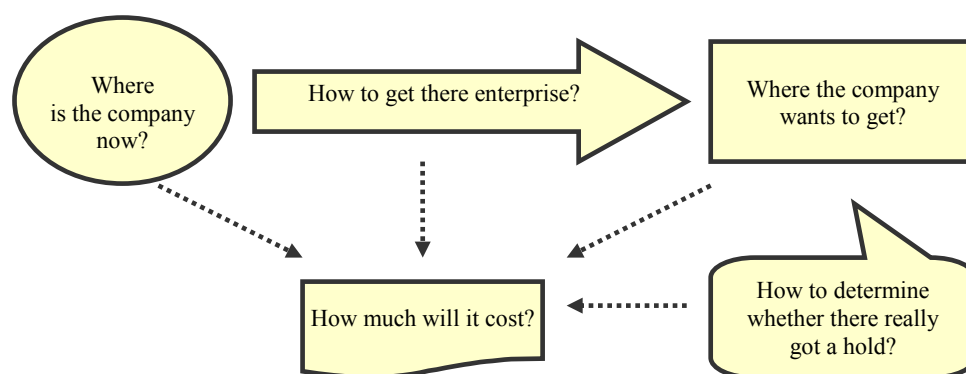
Currently, **the aim of the restructuring** is mainly represented by the following reasons:

- removal of dubious assets,
- optimization of the company value,
- rescue of company
- reduction of costs.

## 6.7 Restructuring programme

The restructuring programme must be clear to all concerned, that the restructuring will deliver, what sacrifice is expected and what would happen if they do not support the restructuring process. When developing the restructuring programme, five basic questions have to be answer (Figure 6.4):

- *Where is the company now? (Starting position)*
- *Where the company wants to get? (Objectives)*
- *How does the enterprise get there? (Activities, methods)*
- *How to determine whether the company really gets there? (Monitoring, evaluation)*
- *How much will it cost? (Schedule, budget)*



**Fig. 6.4** Basic questions in the formulation of the restructuring programme

Restructuring in the recovery of the ompany is executed via the form of a specific type of business projects that are aligned with the restructuring programme.

**Restructuring programme** modifies the course of restructuring, both in terms of content and chronology. According to International Accounting Standard IAS 37, based on the idea of the concept of crisis restructuring, the parts of the restructuring program are:

- identifying the **areas** related to the restructuring,
- determination of the **measures** of planned changes,
- ensuring the **personnel changes** implemented,
- determination of location, functions and number of **workers** who will be given compensation for their employment termination,
- statement of **financial effects** and determination of the costs incurred,
- **timing** of the implementation of the restructuring,
- rules for **monitoring and control**.

The restructuring programme is elaborated in detail into individual **restructuring sub-projects**, usually by type of the business activity. The changes that take place in the enterprise, are usually aimed at various business areas. Nevertheless, individual changes do not operate in isolation, but are closely linked with interactions and bonds among them.

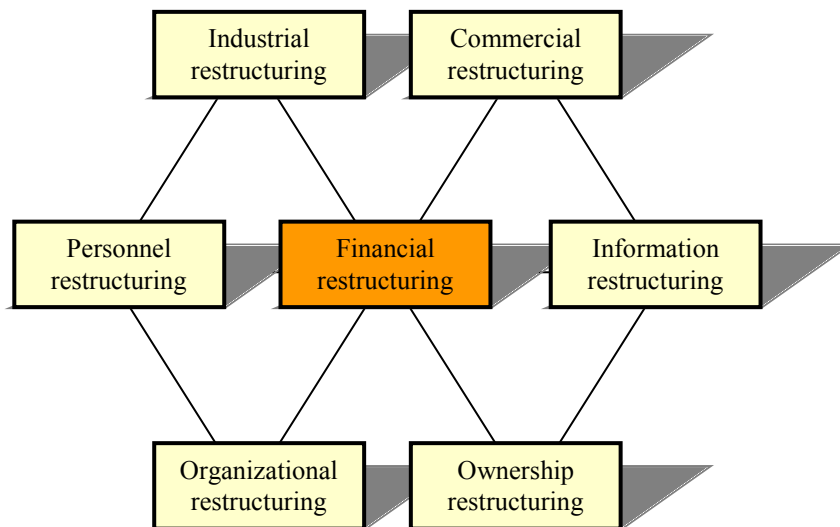
Corporate restructuring is based on the changes that may relate to any aspect or factor of the enterprise. Respective areas and measures of restructuring changes are determined by the nature of the restructuring process. The nature of areas and measures for restructuring changes are determined also by the nature of restructuring.

Restructuring may be focused on different aspects of the company:

- **Restructuring of the reaction** is often affected by source limitations which are often caused by, for example, a fall in turnover, the limitations of the labour force, reducing wages and the like.
- **Strategic restructuring** involves new marketing strategies focused on exports, adaptation and preparation of organizational structures of enterprises.
- **Deep restructuring** includes the formation of long-term strategies that can bring improvements in the company. They usually include the significant investments in capital, technology or know-how.

The process of corporate restructuring in the comprehensive meaning affects all business activities and includes financial, production, trade, information, ownership, organizational and personnel restructuring (Figure 6.5), which form the core areas of the corporate restructuring. For each area of corporate restructuring a specific restructuring project is developed.





**Fig. 6.5** Fundamental restructuring projects [68]

In the process of corporate restructuring the financial restructuring of the key role which arises from the following facts, is met:

- ultimate aim of the restructuring process is represented by the objective that is of financial nature,
- implementation of the restructuring program requires a significant amount of funds,
- financial instruments and measures are applied in each of the areas of restructuring changes.
- implementation of restructuring measures in different areas of business activities always entails some financial implications.

#### **6.7.1 Project of financial restructuring**

In the of financial and property areas it comes to the implementation of measures focused on:

- Improving cash flows that are based on measures of profitability and assets, and to obtain external finance.
- Optimizing financial structure, which consists of respecting the funding rules and principles of optimizing the financial structure.
- Optimizing and streamlining the evaluation and selection of investments, based on the principle of making optimal investment strategy in terms of profitability and liquidity.

Within the financial and property areas the following measures are executed, such as the disposal of unneeded property, rental of excess property, suspension of expenditure on research and development and investment, increase recovery, disposal of assets, liabilities and change in the pattern extension of their maturity.

The first stage of financial restructuring is to clean and **clarify the company's balance sheet** consistently, i.e. the individual items of assets and liabilities. It is the introduction of the

real book value of the business assets, and grasping and covering the maximum amount of potential risks that could arise in the future of recorded or unrecorded assets and liabilities.

**Change of auditors** is needed as well, in order to verify the reality of the economic results of recent years. In addition to comprehensive verification of company financial results the audit should focus on the following, trouble areas in the company balance sheet:

- **Tangible and intangible assets** – to check whether the carrying amount of recorded assets presents fairly the actual condition and wear. It is able to analyze the needs of the property for the conduct of business and prepare the evidence for decisions about the sale of unneeded assets.
- **Non-current financial assets** – in most businesses its value is overstated and does not reflect the real situation.
- **Inventory** – re-assess the fair values of inventory business turnaround and analyze their need for financial coverage by the working capital.
- **Claims** – it is necessary to make real way of checking the receipts and recoveries.
- **External resources** – not only make value of loans and commitments real, but also the reserves and unrecorded liabilities.

Following the operations of **revaluation of the balance sheet**, it comes to the display of their results into the result of profit or loss for the related accounting period. In most restructured businesses the value is exceeded by the amount of capital losses. In these cases usually it is not enough to reduce the share capital by the amount of the loss incurred, but it is necessary to proceed to the capitalization of the share capital by obtaining additional resources.

Restructuring of the balance sheet should be positively perceived by all partners of the company, despite its impact on the equity of the company, which leads to more realistic actual state of the business. The introduction of real balance sheet shall be presented to the public in the right way, to avoid the considerations of the economic situation deterioration of the company being restructured. It must be explained that this is only the first step that leads to improving the situation of the company.

The next step is to achieve **transparency in accounting**, in management accounting in particular. It is necessary to introduce reporting, controlling and management information system that provides the right information at the right time.

One of the objectives of financial restructuring must be represented by **minimizing the costs associated with loan financing**. Foreign sources of business can be divided into two groups, each group of liabilities requires a specific approach:

- **Bank loans** whose conditions for granting and repayment depends on the financial situation of the company. Minimizing of costs should be achieved by enhancing the flexibility of short-term resources and strengthening the foreign currency loans in total financing. It is necessary to replace the part of short-term loans to medium-term loans, especially in cases where the portion of long-term assets is financed by short-term resources. Furthermore, it is necessary to eliminate most of the long-term financial assets and unneeded assets of the company. The medium-term objective of financial restructuring

is represented by progressive reduction the volume of existing loans, thus creating the conditions for the financing of future development projects in the company.

- **Trade payables** that are overdue, should be paid as soon as possible. The payment plans are devoped to assist in the planning of cash flows. In the existence of assets and liabilities within a specific group of enterprises it is essential to use mutual credits and find a suitable calculation chain and sometimes use the services of specialized companies.

### **6.7.2 Production restructuring project**

In the production area, the attention is mostly focused on the structure of the production programme, structure and quality of production-technical base, preventive care of production equipment, production process, quality assurance and improvement, innovation, changes management oriented on the product where it is possible to include the costs reduction, the increase of result quality, shortening of production time, distribution, new product development, sorting or removal of unproductive time.

In the production area it is mainly the reduction of production capacity and adapting it to the production structure and volume of customer's requirements.

The basis of production restructuring is to carry out **an audit** of each **core activities** of the company. This part of the restructuring should be carried out in cooperation with specialized companies that focus on checking the basic company functions in a particular industry.

One of the optimal methods for auditing the basic functions is represented by the benchmarking method. The analysis is divided into two stages:

- In the analytical part, the specific key activities are investigated by an external team of experts to identify the shortcomings in the activity. The audit involves the direct participation of judges in specific company processes and interviews with staff. The output is via the summary report, which highlights the shortcomings and proposes the framework for handling certain troubles. The report is discussed with senior management to determine the procedure in the second stage.
- The second stage is aimed at the transfer of analyzed key activity to the level of an international standard, which is common among other competitors in the field given.

The analysis should address the basic trouble areas of company individual key activities. In cases of extreme urgency, it is possible to achieve the fastest effects via restructuring the purchase and inventory management in the company.

### **6.7.3 Project of business restructuring**

In the business area the attention is mostly focused on the customer. There is an ongoing monitoring, evaluation and adaptation to customer needs, creating the atmosphere in the company, which is for the benefit of customers and building partnerships with customers. New methods and procedures for commercial activity are formed and applied. To join the e-commerce is an opportunity for many businesses.

Project of business activities can be divided into the part of purchasing and sales activities.

- ***Project of purchasing activities***

The most common deficiencies in purchasing can be summarized as follows:

- high proportion of administration that does not bring any value
- large number of offers and demands conducted orally without a credible record
- close connection with a limited group of suppliers,
- preference of suppliers who are geographically closest to the company, despite that it is uneconomical for the company,
- division of the purchasing department into the raw materials purchase of and services purchase sections.

The basis for the restructuring of the purchasing department is to define the activities of the purchase and supportive administrative staff:

- **Activity of purchasers** should consist of the following activities:
  - good knowledge of the market with an emphasis on knowledge of direct producers, distribution channels and the underlying business conditions,
  - personal negotiation of individual contracts and identification of major contracts,
  - rapid conclusion of the selected transaction.
- **Activity of administrators** should focus on technical support of closed transactions including transport, insurance and inspection. The administrator should never represent the purchaser.

The purchasing team should be organized according to the different groups of products purchased in combination with the specialization in a certain territory. Groups of purchased products should be divided into different subgroups according to their value and the number of items using the ABC method. The main criterion for distinguishing the competitive offers should be represented by the price. The purchasing team should be dynamic and responsible for inventories.

- ***Project of sales activities***

Sales activity is mostly the weakest link in the enterprise and its restructuring is extensive and time consuming. The fundamental issue of enterprises in the field of sales can include the following factors:

- no real sellers operate in the enterprise, the sales and marketing activities are not carried out,
- scope of products is large, and therefore it is appropriate to:
  - consider the possibility of selling only the products with higher added value,
  - focus on products that are promising for the enterprise,
  - try to get the advantage of from the scope of products,

- use questionable intermediaries or brokers owned and controlled by friends and colleagues.

#### **6.7.4 Project of personnel restructuring**

In the first stage there is a complete or partial **replacement of the statutory bodies** of the company. Personnel changes in the statutory bodies and corporate management are motivated by obtaining the rapid and effective control over the whole company process, and without their consistent and effective application, the restructuring is not feasible. The changes in the senior management demonstrate the strength and willingness to penalties within the responsibility for the state in which the company is. The change at the highest company levels has a positive psychological impact on the further development of the restructuring from the perspective of the middle and lower management. The reason for the personnel changes are represented also by planned restructuring measures, which cannot be done with the same management.

In the next stage of restructuring the personnel audit of the restructured company is done with the assistance of an external personnel consultant. The reason for the use of external access is to ensure an uninterested perspective from the outside and ensure the independence on the existing personnel relations in the company. The audit objective is to optimize the structure of human resources in the company in terms of number of employees. It includes a proposal for measures to improve the systematic work as well as the proposal of the development of key people for the future of the company.

#### **6.7.5 Project of restructuring the organizational structure**

In the organizational area there is the effort to form the simplest internal structure of the company, both in terms of granularity, hierarchy, and communication links, adaptable organizational forms able to quickly and flexibly respond to changing conditions. The company is required to implement the changes in business processes and form the enterprise process organization. Other possible changes are represented by the expansion or narrowing the cooperation with outside consultants, or by the use of outsourcing and doublesourcing.

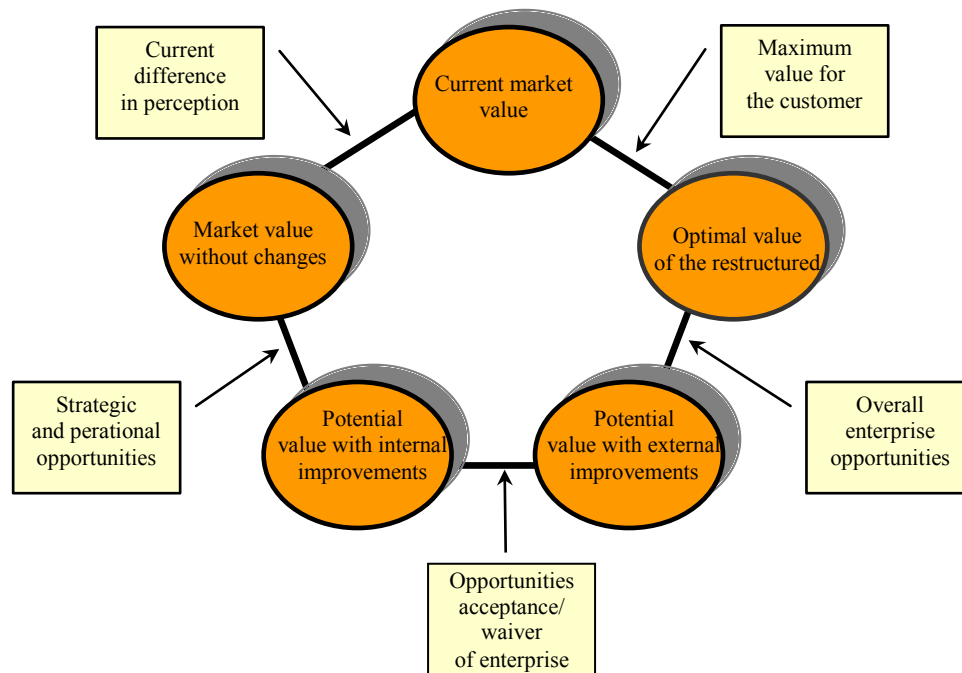
In most enterprises being restructured, in relation to other areas of restructuring, large changes in the organizational structure must be made. The need and necessity of changes relates to making the unclear organizational hierarchy more comprehensive, since it does not meet the basic requirements for a functional organization. The new organizational structure must show obvious material flows, energy, information and financial resources.

The new organizational structure should centralize the key fundamental business activities, if they are advantageous. In most restructured enterprises it is beneficial to form a specialized section of purchase, production and sales. The effective centralization allows the consistent use of the advantage of scope, which may be very significant.

#### **6.7.6 Project of restructuring the ownership**

In relation to the changes in the ownership structure it is necessary to know the value of the business before and after the change. Exploring the value of the company can be addressed in different ways. One possibility is to identify and manage the value of the

company through the restructuring pentagon (Figure 6.6), which comprehensively perceives the whole issue of the value management.



**Fig. 6.6** Pentagonal framework for determining the restructuring opportunities [130]

When analyzing the value of the company it is necessary to examine the performance of the business in terms of the shareholders and from the aspect of the current company market value. To determine the market performance, we can use the analytical framework comprising:

- **Review of market performance** – determining the income for shareholders compared to other investments.
- **Analysis of the performance of comparable companies** – forming an initial picture of the company performance, which is the basis of market performance.
- **Understanding the cash flows** – determination where the company forms and invests cash and find what yield this investments produce.
- **Findings of market insights** – identifying the assumptions forming the present company value.

After the pre-restructuring analysis thorough overview of the state of the portfolio and value creation opportunities based on facts is available. It also is found, what is the risk of the takeovers. In the Slovak Republic a violent takeover or transposition of a company is not very frequent. In Europe and the U.S. it is a common procedure, how to obtain the control over the other company. Therefore, the risk of takeovers is taken very seriously, and for any analysis of the company focused on the long-term development in the future, this risk is analyzed and barriers to prevent a hostile takeover are formed.

The changes in the ownership structure occurs in the purchase and sales of a company under contract of the sales of assets, of non-cash contribution to a company, capital increase

by issuing the Units, then by the merger, the division of the company, by the offer of the takeover and the like.

The need for a major corporate restructuring occurs at the emergence of the big gap between the actual and potential company performance. The purpose of the corporate restructuring is to increase the value of the company. It is the strategy of searching and forming the incremental value. The value of the company is mainly influenced by the following four main groups of factors:

- **Sum of corporate property prices**, which tells you how much capital would be spent to build a company with equal opportunities.
- **Financial structure of the company**, which indicates the proportion of equity and loan capital to cover the operating assets.
- **Current and expected return**, a crucial factor influencing the company value.
- **Intrinsic value of the company**, which comprises the action of a variety of non-material factors that cannot be clearly quantified, such as quality management, training of qualified staff, well run organization of production, relations with suppliers, built distribution channels, company reputation, value of patents and licenses, brand value, favourable territorial allocation and others.

The negative factor affecting the value of a business can include:

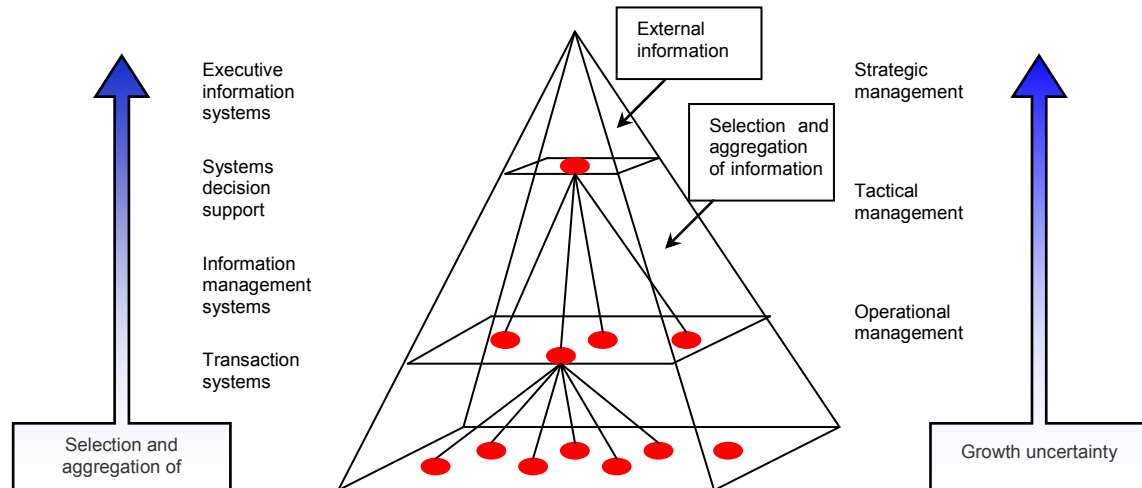
- elimination of the benefits of company size,
- unstable and turbulent environment,
- loss of benefits from the integration.

Immediate results of restructuring may have a different scope, size and costs associated with reaching the desired results.

#### **6.7.7 Project of information restructuring**

Restructuring project of the information area should be focused on forming an appropriate structure of information and communication systems that will support decision made by providing the relevant information.

Regarding the level of management to which the information system provides information, it is possible to subdivide the enterprise information system into certain subsystems, each of which performs its functions. For each level of management, there are software applications that perform the required functions of the level, hence the information pyramid is formed (Figure 6.7).



**Fig. 6.7** Information pyramid

Quality enterprise information system should cover all three levels of management, strategic, operational and tactical. Only an integrated and holistic enterprise information system can be really effective.

One way to tackle the information needs of management is represented by the corporate reporting, which can be considered one of the oldest tools of management information systems. It can be defined as a semi-automatic business process or functionality providing the information required on a regular or occasional basis. Regular reporting mostly relies on predefined schemes and occasional (ad-hoc) reporting responds to specific user queries.

Due to the changing environment and information management needs in terms of management there is an increasing interest in particular forms of ad-hoc reporting. This can occur in two forms:

- **On-demand reports** represent non-standard reports, formed at the request. The content and presentation is easier and more accurate. The response time between the request and the report is longer, but the output quality is very high. They are supported by data mining technologies.
- **Online reports** are reports that are formed by directly by the managers based on their current information needs. It is a comprehensive and more prompt method of obtaining information as the information technicians are not involved in the process. They are supported by OLAP and Business Intelligence technologies.

Since the future business results, business environment and competition is now predictable only with a certain degree of probability, in the information and communication technologies the managers lay increased demands not only on the quality but also on the interpretability of the information needed for management decisions.

## **6.8 Timetable of restructuring**

Timetable determines the duration of each step in restructuring the company and determines the total duration of the restructuring. Scientific studies indicate that the average duration of corporate restructuring is two to three years.



For establishing the schedule of restructuring it is possible to use different methods, for example, the logical framework (Table 6.2) or Gantt chart.

**Tab. 6.2** Pattern timetable corporate restructuring

Order of tasks	Workload	Responsibility/ implementation	Week of implementation
1.	Finding a state of crisis	management	1
2.	Determine the extent restructuring company	management	1
3.	Assembling the team	management	2
4.	Framework plan for corporate restructuring	head of the restructuring team	3
5.	An in-depth analysis of the company	restructuring team	4–6
6.	Defining problems and their causes in the enterprise	restructuring team	7
7.	Defining the vision and strategy of the company restructuring	management restructuring team	8
8.	Defining the main and auxiliary objectives of restructuring	management restructuring team	8
9.	The preparation of the restructuring program	restructuring team	9–12
10.	Presentation of the management company	head of the restructuring team	12
11.	Implementation of corporate restructuring – implementation of measures restructuring projects	management restructuring team	13–50
12.	Continuous control tasks and schedule compliance restructuring	management restructuring team	13–50
13.	Incorporate corrections to the restructuring program	management restructuring team	13–50
14.	Final evaluation of the achievements of the restructuring	management restructuring team	51–52

In the schedule of the restructuring it is necessary to indicate the duration of the actions and responsibilities of the different members of the restructuring team.

## **6.9 Budget of restructuring and financial effects of restructuring**

For the period across the entire corporate restructuring it is necessary to develop a budget of restructuring. The budget is established for each year of the restructuring, or for shorter periods of time, e.g. half-yearly or quarterly.

The basic structure of the budget is as follows:

- **costs budget**
- **budget revenues,**
- **cash flow plan.**

In developing the **budget of expenses**, various restructuring projects and activities that have been planned in the restructuring programme can be considered. The basic items in the costs budget are:

- costs for individual restructuring projects,
- costs for severance for employees,
- costs for external collaborators in the restructuring team.

When preparing the **budget of revenues** we plan also the revenues from the sales of unneeded assets. A sample budget of costs and revenues is presented in Table 6.3.

**Tab. 6.3** Sample budget of costs and revenues of restructuring

Item			Year of restructuring			Together
			1. year	2. year	3. year	
Severance costs	Technical and administrative staff	Severance				
		Number of persons				
	Labor	Severance				
		Number of persons				
	Together	Severance				
		Number of persons				
Costs of restructuring projects	Financial restructuring					
	Industrial restructuring					
	Commercial Restructuring					
	Personnel restructuring					
	Information restructuring					
	Organizational restructuring					
	Ownership restructuring					
	Together					
Payroll costs for external collaborators restructuring team						
Other costs						
Total restructuring costs						
Proceeds from sale of assets						
Other income						
Proceeds restructuring together						
Profit from restructuring						

The difference of revenues and costs represents the **profit from restructuring**, which is mostly a loss. If necessary, it is possible to specify the financial effects of restructuring closer.

When **planning the cash flows** we have to consider the restructuring programme in terms of time and subject matter, then the budget of cost and budget of revenues. It is necessary to consider also the material and disproportion of expenditure and costs and earnings and revenues.

Budget of restructuring should be developed by the member of the restructuring team who is experienced in the implementation of restructuring programmes in other businesses. Each restructuring project is unique, so there is no universal procedure for forming the budget and determination of the amount of restructuring costs, revenues, income and expenses. The most common procedure is to use a qualified estimate.

## 6.10 Projection of the company plan after restructuring

The planning of the desired condition that the company wants to achieve via the implementation of the restructuring is the part of the restructuring programme. The project plan of the company after the implementation of the restructuring should include the following sections:

- **projected balance sheet,**

- **projected income statement**
- **projected cash flow statement.**

The **business plan** or **production plan**, specifying certain balance sheet items in detail, such as the amount of inventory items and income statement, e.g. sales of own products and services and the like can be the part of the projection.

### **6.11 Implementation of restructuring**

Contents of the implementation stage of restructuring is as follows:

- Implementation of measures specified in the individual restructuring projects.
- Continuous checking of tasks implementation and compliance with the timetable for the restructuring.
- Incorporation of corrections into the restructuring programme, if necessary.

The aim of managing the restructuring projects is represented by the organization and management of work in the project so that the project Schedule is met, and thus the objectives of the restructuring are achieved. In the implementation of the restructuring it is necessary to harmonize the implementation of measures of individual restructuring projects.

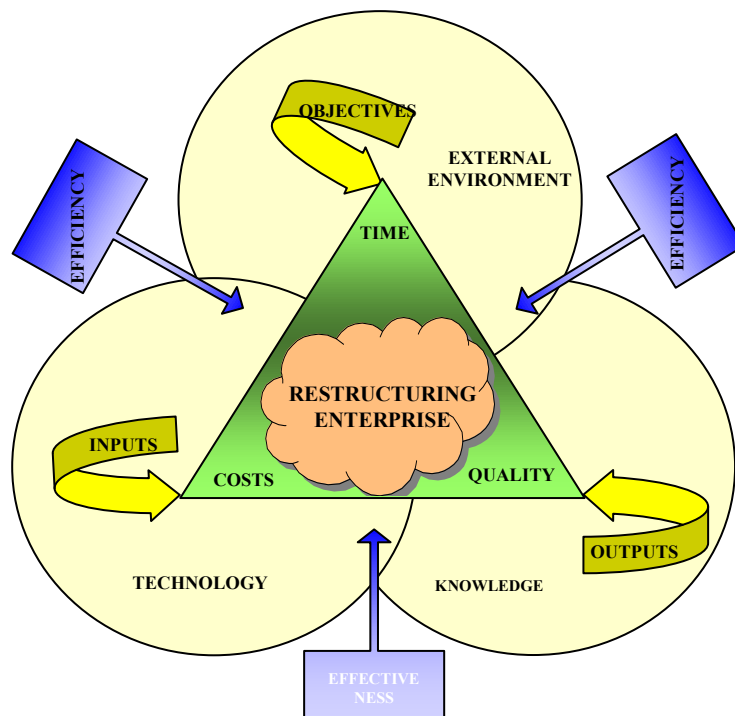
One of the challenges in the restructuring implementation is to monitor the risky events and manage the changes which can result due to them.

There are essential prerequisites for successful implementation of the restructuring:

- Qualitative thorough analysis of the situation in the company before the start of the restructuring.
- Understanding the true state of the company.
- Developing a strong interest in the company recovery and involve the management in the restructuring outcome so that the company is functional and coherent.
- Building of quality restructuring team, which consists of key managers, who must be able to work in a team and take and implement tough and unpopular decisions.
- Determining of correct restructuring priorities.
- Identifying clear objectives for restructuring and responsibility for specific tasks.
- Constantly encouraging and motivating the employees via using open communication and corporate values and principles of negotiation.
- Gaining the trust of customers who in the period of the crisis are susceptible to change the supplier because the company's ability to survive is threatened as well as its delivery capabilities.
- Restoring relations between the company and its most important stakeholders, such as banks, customers and employees.
- Stabilizing the achievements in business.

Controlling of the ongoing restructuring projects allows detecting the status of the project implementation. The subjects to the control (Figure 6.8) are as follows:

- **project time schedule** – meeting deadlines,
- **project budgets** – withdrawing the costs, use of resources, achievement of revenues,
- **quality** – the results quantity and quality of individual activities and projects.



**Fig. 6.8** Magic triangle of time, cost and quality of corporate restructuring

The actual performance within the restructuring projects is measured by detecting the information on the project status, meeting the deadlines, withdrawing the costs and use of resources and the quality and quantity of the results obtained. The information is collected from project documentation, or from other sources, such as from the observation.

As for meeting the deadlines, the beginning, end, and degree of operations completion according to the planned timetable and as well as the dates of achieving the partial targets in comparison to current dates are checked. The existence of deviations do not always require an immediate corrective action. If there in the activities of the deviations is a reserve, and therefore the resulting deviation does not endanger the implementation of other planned activities, the correction is not necessary.

Each restructuring project should also include a **risks management plan**, which includes the definition, forecasting, monitoring and limiting the consequences of forming the risk events. The principal risks can include:

- **time** – overrun of the time limit for achieving the project results,
- **costs** – overruns of projects budget,
- **quality** – results of the projects were not implemented in the planned quantity or quality.

The objective of the risks management project planning is to minimize the negative consequences of risks at events.

After the implementation of all the restructuring measures it is necessary to terminate the restructuring:

- conclude the project documentation,
- prepare technical and financial report of the project,
- prepare the plan to transfer experience and knowledge gained in the restructuring project for the purposes of other projects,
- evaluate the work of the restructuring team,
- dissolve the restructuring team.

## **6.12 Evaluation of the results of the restructuring**

Evaluation of the results is an integral part of the restructuring, and focuses on finding answers to three basic questions:

- Were the restructuring projects implemented correctly?
- Were the desired results of restructuring projects achieved?
- Was the objective of the company restructuring reached?

The first question focuses on the implementation of restructuring projects, manage cost, time and quality and is closely associated with the control. Evaluation at this level takes place during the implementation of restructuring projects.

The answer to the second question is determined at the end of each restructuring projects at the moment of achieving the results. The evaluation of projects is related to their planning, since during the planning the measures and actions to ensure they achieve the desired results were determined.

The third question deals with the strategic level. The projects are an instrument of strategy implementation and evaluation of corporate restructuring at this level, and they show to what extent restructuring projects support the achievement of corporate restructuring.

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