Managing crisis of SMEs with restructuring projects

Igor Vrečko, PhD¹ and Karin Širec, PhD²

Abstract
While small and medium-sized enterprises in Slovenia, as well as in EU, constitute more than 99% of European enterprises, they are similarly vulnerable during economic declines as we are facing it since 2008. The paper deals with crisis management challenges in SMEs, focusing more on the strategic instead of business crisis. Projects based restructuring processes are presented as a suitable form for dealing with strategic crisis. Seven types of restructuring projects have been identified. Based on the characteristics of strategic crisis as well as on restructuring projects specifics of SMEs, a conceptual framework for dealing with strategic crisis is proposed. Specific of the model is its two-dimensionality, consisting of systemic and processing dimension for mastering restructuring projects in crisis situations.

Key words: crisis management, restructuring, project, project management, SMEs

INTRODUCTION
Small and medium-sized enterprises (SMEs) constitute more than 99% of European enterprises and account for about 2/3 of private sector employment and 50% of the value-added created by businesses in the European Union (EC, Facts and figures analysis). Turner et al. (2009) have shown that projects account on average for one third of the turnover of SMEs, and thus projects in SMEs account for almost one fifth of the economy.

Like large companies, SMEs are subject to restructuring which is a general characteristic of economic development and often a consequence of crisis appearance in firms. Structural change, driven by shifts in relative productivity and demand, technological or socio-economic changes, is a tool to adapt to the altered framework conditions and therefore necessary, not only to guarantee stable and growing market economies but also to sustain and improve living standards of the population (Storrie 2006). However, restructuring is seldom a smooth and painless process. The nature of project management required by SMEs is very different than the traditional forms of project management suggested for larger projects and since today very little is written about the project management requirements of SMEs (Turner et al. 2010). A very prominent recent example for restructuring are the adjustments companies were taking to cope with the global economic and financial crisis. In Slovenia for example, the majority of restructuring measures are targeted at companies experiencing serious performance problems - loss of markets, financial problems, reduced employment or being at the edge of bankruptcy. The majority of publicly discussed restructuring cases involve large companies and companies in difficulties. SMEs are not the focus of public interest to the extent they deserve. The recent crisis, for example, has shown that in the short-run, the economic and employment situation in smaller firms is more stable than in larger enterprises (EIM 2010). Compared to larger firms, smaller enterprises tend to maintain more employment above the efficient level in downturns as they have fewer opportunities to lay off personnel while at the same time having stronger personal ties with their employees (Voss 2007). In the medium-run, however, effects are more severe and long-lasting for smaller companies.

Unfinished transitional process, and relatively poor main economic indicators compared to EU (presented in the following section) are reasons why Slovenian firms facing considerable challenges in managing their restructuring projects in crisis situations. The purpose of this paper is to present the diversity of crisis emergence in companies. We provide a set of potential restructuring projects and highlight the characteristics and particularities of SMEs. In the two-dimensional model, we define the necessary process and system requirements for the mastering of strategic crises with restructuring projects of SMEs.

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COUNTRY CONTEXT
To give an overview of restructuring processes in Slovenian SMEs, we need to identify important features of the political and economic context Slovenia (and similar transition countries) has faced in the last two decades. We are going to describe macro-level restructuring processes as well as key economic indicators, helping to understand better the wider framework within which SME restructuring takes place. To provide insight into micro-level developments in SMEs, we present business statistics comparing Slovenia’s SME sector with the EU-27 (Širec and Rebernik 2012).

Since starting life as an independent state in 1991, Slovenia—with a population of two million people—has had to make two fundamental restructuring transitions: to an independent country and from socialism to capitalism. At the dawn of this new era, the economy was characterized as a ‘socialist black hole’ (Vahčič and Petrin 1990, 69) because of the almost complete absence of small companies with 10-100 employees. By restructuring the Slovenian economy, this black hole was filled in two ways: from the top down with spin-offs and the remnants of bankrupt large companies; and from the bottom up with emerging start-ups and growing micro and small companies contributing to employment.

Economic indicators show that transition processes are still not complete with the recent recession slowing them down further (Kedmenec et al. 2011) (Table 1). The global financial and economic crisis seriously affected the Slovenian labor market, with numbers in paid employment decreasing significantly. The employment rate in 2008 was 68.8% (Kresal 2010). In 2010 the employment rate declined for the second year in a row but remains above the EU average. It was at 66.5% in the second quarter of 2010. Particularly the employment rates of young people aged 15–24 and people aged 25–54 declined in 2009 and 2010, while the employment rate of those aged 55–54 is steadily increasing. Also in 2010, the employment rate mainly dropped due to the contraction of formal employment, which was most pronounced in manufacturing and construction (UMAR 2011, 146).

Table 1. Main economic indicators in Slovenia

<table>
<thead>
<tr>
<th>Indicator</th>
<th>Value</th>
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<tbody>
<tr>
<td>Real GDP growth</td>
<td>-8.1</td>
</tr>
<tr>
<td>GDP (in € mil.)</td>
<td>35,870</td>
</tr>
<tr>
<td>GDP per capita (€)</td>
<td>17,657</td>
</tr>
<tr>
<td>Consumer Price Inflation</td>
<td>0.9</td>
</tr>
<tr>
<td>Unemployment rate</td>
<td>5.7</td>
</tr>
<tr>
<td>Total population (in millions)</td>
<td>2.0</td>
</tr>
</tbody>
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1) Bank of Slovenia, Statistical Office of the Republic of Slovenia (data for the year 2009)
Source: Kedmenec et al. 2011

Small Business Act (SBA) Fact sheets 2010/2011 show that Slovenia’s SME sector closely resembles the EU’s (Table 2). The most notable deviation from the European pattern is that, while employing fewer people—64.2% of the workforce in the business economy compared to an average of 67% in the EU—Slovenian SMEs produce proportionately higher value added (63% vs. 58%). This means that the labor productivity differential between small and large businesses is smaller in Slovenia than in the EU.

Slovenian SMEs also resemble the European average, with only slightly higher concentrations of SMEs in manufacturing (15% vs. 11% in the EU) and construction (19% vs. 14%) and a lower share of small and medium-sized businesses in trade (22% in Slovenia and 33% in the European Union). Like all EU economies, Slovenia has been affected by the global financial crisis and is now gradually recovering, along with the rest of the EU. The crisis has taken its toll on Slovenian SMEs, temporary halting the positive long-term trend in their contribution to employment and to economic value added. The workforce employed by SMEs experienced a sudden drop from 2007 to 2008, but has since stabilized. Behind this aggregate picture, sartorial trends differ, with SMEs in manufacturing and trade being the worst hit, having laid off 16% and 14% of their employees after the sharp drop in external demand.
Table 2. SMEs in Slovenia and EU27 – basic figures³

<table>
<thead>
<tr>
<th></th>
<th>Number of Enterprises</th>
<th>Employment</th>
<th>Value added</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Slovenia EU27</td>
<td>Slovenia EU27</td>
<td>Slovenia EU27</td>
</tr>
<tr>
<td>Micro</td>
<td>99,057 92,6% 92,1%</td>
<td>174,480 27,8% 29,8% 4 22,3% 21,6%</td>
<td></td>
</tr>
<tr>
<td>Small</td>
<td>6.381 6,0% 6,6%</td>
<td>110,816 17,7% 20,4% 4 19,9% 18,9%</td>
<td></td>
</tr>
<tr>
<td>Medium-sized</td>
<td>1.282 1,2% 1,1%</td>
<td>117,696 18,7% 16,8% 4 21,1% 17,9%</td>
<td></td>
</tr>
<tr>
<td>SMEs</td>
<td>106,720 99,8% 99,8%</td>
<td>402,991 64,2% 66,9% 11 63,2% 58,4%</td>
<td></td>
</tr>
<tr>
<td>Large</td>
<td>253 0,2% 0,2%</td>
<td>224,748 35,8% 33,1% 7 36,8% 41,6%</td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td>106,973 100,0% 100,0%</td>
<td>627,739 100,0% 100,0% 18 100,0% 100,0%</td>
<td></td>
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</tbody>
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STRATEGIC AND BUSINESS CRISSES

Among first researchers who spoke about the importance of crisis appearance for the strategic development of firms was Krystek (1987). He divided crisis into operational (we also talk about business crises) and strategic crisis. Strategic crisis was defined as false detection, recognition and/or anticipation of changes in the business environment that have a direct or indirect impact on the firm’s future operations and competitiveness, and on this basis defining wrong strategic direction for firm’s and their implementation.

Relatively few other authors dealing with strategic crisis define them based on a Krystek definition. Thus, for example, Blatz and Haghani (2000) define strategic crisis as failure to provide long-term potential performance and achieving strategic objectives, leading to declining competitiveness of the company. Hauc (2002) sees it as a particular form of crisis which does not have a direct impact on the business disruption or immediate occurrence of operational crisis, but will have consequences in the future, when a company should operate in a manner that should be result of adjustments to the strategically changed environment. Vrečko (2002) talks about strategic crisis when the company lags behind with the preparation and implementation of the necessary strategic adjustment of their business according to the changes in the external and internal environment.

Strategic crisis occurs at a strategic gap that occurs between the changing business environment and not (enough) adjusted enterprises (Richardson et al. 1994). Change in the business environment may present the direct threat for the company (e.g. the emergence of a new competitor, a better competing product, etc.), but it can also be an opportunity (e.g. the collapse of a competitor and thus the opportunity to enter markets, changes in customers’ habits, etc.). Whether a change represents a direct threat or an opportunity, an inadequate response to it leads to a deterioration of the company, as neglected or unexploited opportunities in the current competitive and global business environment certainly soon will be exploited by competition.

In the exponent changing dynamics of the modern business environment, each company almost permanently faces the danger of a strategic crisis emergence. Kash and Darling (1998) argue that it is not an issue, whether a company is going to face with a crisis, but when and in what form will it appear, and more importantly, how the company is ready to cope with it. Businesses of all shapes, ages and sizes are going to be at some points in their life cycle faced with the changes that have the potential to lead to a crisis of different dimensions (Ritchie 2004). This is why the implementation of restructuring projects in different forms inevitable becomes a phenomenon in all phases of the company’s life cycle (Hauc et al. 2011).

If the company had no control over strategic crisis successfully and timely, it is usually followed by operational business crisis. This may also occur for other reasons (e.g. natural disasters, major defects in

³ Estimates for 2010, based on 2002-2007 figures from the Structural Business Statistics Database revised (Eurostat). The estimates have been produced by Cambridge Econometrics. The data cover the ‘business economy’ which includes industry, construction, trade, and services (NACE Rev. 1.1 Sections C to I, K). The data does not cover agriculture, forestry, fishing or largely nonmarket services such as education and health. Eurostat data are harmonized and comparable across countries. The disadvantage is that, for some countries, data differs from that published by national authorities (EU, SBA Fact sheet Slovenia, 2010/2011, 1).
production, etc.), but the most common precursor of operational crisis is strategic crisis (Vrečko 2002, Haghani 2004).

Operational crisis is the kind of crisis that we have most often in mind when talking about the crises in the company. They typically can be recorded and are often seen in the decline of company’s indicators (e.g. decline in sales revenue, market share, or profit, customers leaving to competitors, etc.). Mastering of such crises is usually laborious and time consuming process, especially because of the evidential problems often resulting from deeper (strategic) problems that management of companies often (too) long pushed into the background, especially if for any reason (deliberate or accidental) they are also objectively responsible for a crisis.

On the other hand, the strategic crisis can hardly be detected with certainty or be confirmed until they already pass over into operational crisis. Therefore the likelihood that the company will holistically and timely solve strategic crisis is rather low, since usually they are not confident enough that the company is strategically compromised. Finding ways to mastering strategic crises should be focused to analyze and mastering of strategic causes of the crisis. This should be the starting point of the identification and implementation of restructuring projects.

Shrivastava and Mitroff (1987) as well as Smith (1992) believes that much of the operational problems in the company derive from the previous errors in the processes of strategic management. Haghani (2004) survey revealed that the most common cause for operational crisis derives from the errors made in the development of the company. Similarly, Hauschildt’s (2006) study showed that the strategic crisis often occurs due to insufficient holism and often too short time horizon when thinking about the future of the company.

Thompson (1998) identifies the characteristics of enterprises indicating their tendency to development of the crisis. We can actually speak about causes for the emergence of strategic crises, among which we highlight:

- Lack of holistic thinking and action across the company or its individual parts,
- Inability to cope with changes or resistance to them,
- Failure to properly and adequately interpret environmental signals.

In dynamic business environment companies’ management is often faced with various strategic dilemmas that have potential to cause changes in their existing strategic orientation. Therefore, the inadequate strategic actions or inadequate dynamic of strategic actions - when compared to the intensity change of the business environment - will soon lead to the occurrence of operational problems. Blatz and Haghani (2000) pointed out that the failure in the implementation of the corrective actions aimed to solve emerged strategic crisis leads to the occurrence of operational crisis.

Based on various problem areas of mastering the strategic crisis, we can actually define two groups of problems that need to be addressed to ensure success in mastering the strategic crisis and implementation of restructuring projects. The first group refers to the process problems for mastering strategic crisis, which is about 1) detect, analyze and interpret changes (threats or opportunities) that take place in the business environment of the company and have a relevant impact on the implementation of existing and future business processes, and 2) the design, selection, and effective realization of the relevant restructuring projects and other measures necessary to maintain or improve the company’s competitiveness in relation to changes in the business environment. The second group refers to the system problems for mastering strategic crisis, which is about the company’s ability to use its organizational structure, personnel and established way of thinking to master the strategic crisis restructuring projects; it is about 3) the holism in performing operations and sufficient consideration of connections and interdependencies between projects, actions and phenomena, and about 4) an appropriate level of commitment and the necessary creativity, inventiveness and innovativeness of all those who directly or indirectly participate in the company’s restructuring projects.

**TYPES OF RESTRUCTURING PROJECTS IN SMES**

Restructuring comprises a multitude of different forms of reorganizing activities in a company. Some of them have a strategic, proactive character (like preparing for planned growth or diversification) while
others are more reactive and operational (for example, dealing with crisis situations). Quite often, restructuring is rather equaled to the latter, being related to forms of restructuring resulting in job losses, such as bankruptcies, closures or off-shoring. However, even if considering also positive restructurings, it needs to be considered that such changes in most cases constitute major events within the company that rarely are smooth and painless processes and have serious consequences for both, the organization and its workforce.

The European Restructuring Monitor (ERM) of the European Foundation for the Improvement of Living and Working Condition refers to seven main types of restructuring:

- Relocation: When the activity stays within the same company, but is relocated to another location within the same country.
- Outsourcing: When the activity is subcontracted to another company within the same country.
- Offshoring/delocalization: When the activity is relocated or outsourced outside of the country’s borders.
- Bankruptcy/closure: When an industrial site is closed or a company goes bankrupt for economic reasons not directly connected to relocation or outsourcing.
- Merger/acquisition: When two companies merge or during an acquisition which then involves an internal restructuring program aimed at rationalizing organization by cutting personnel.
- Internal restructuring: When the company undertakes a job-cutting plan which is not linked to another type of restructuring defined above. This type of restructuring, however, also refers to internal reorganization that not necessarily result in the reduction of the number of employees, such as business transfers and succession, reorientation of the business purpose, diversification resulting in redeployment of employees or similar.
- Business expansion: Where a company extends its business activities, hiring new workforce. This includes, for example, insourcing or internationalization.

Not all of these types of restructuring are equally relevant for SMEs as for larger firms. Ghobadian and Gallear (1997) described differences between SMEs and larger organizations in dealing with project management processes. They identified peculiarities in 1) Processes: SMEs require simple planning and control systems, and informal reporting; 2) Procedures: SMEs have a low degree of standardization, with idealistic decision making; 3) Structure: SMEs have a low degree of specialization, with multi-tasking, but a high degree of innovativeness, and 4) People: Because of the high consequence of failure, people prefer tested techniques. In spite of the heterogeneity among SMEs and among individual restructuring projects, some typical elements for SMEs in restructuring can be identified (Širec and Rebernik 2012a):

- Most of the SMEs are managed by a single manager/owner rather than a management team. The smaller the company, the stronger is the position of the owner/manager. Consequently, the owner/manager also has a core position in the restructuring project. His/her personal attitude towards and perception of change, management style and competences/knowledge will strongly influence whether, when and how restructuring takes place.
- Furthermore, it must not be forgotten that in many cases there will also be a strong overlap between the personal sphere of the owner/manager and the business sphere, such as that business restructuring might also affect the personal assets of the owner/manager or that family members or friends formally or informally may influence business decisions.
- The restructuring event is often realized in a less anticipated, planned and strategic way, rather ad-hoc and reactive than preventive. This is at least partly caused by the greater difficulties of SMEs (compared to large scale companies) in getting access to (relevant) information.
- Compared to larger firms, SMEs dispose of less financial and human resources. Consequently, less money, time and expertise/organizational specialist knowledge is available to handle the restructuring project. While due to their smaller size SMEs are able to react more flexibly to altered framework conditions, these limited resources hamper the full potential of this flexibility. SMEs, for example, often have fewer possibilities to look for alternatives to or within restructuring or limited access to external support.
- There tends to be a negative relationship between company size class and social responsibility. The smaller the firm, the higher is the owner’s/manager’s commitment towards his/her
employees, caused by tighter personal links, resulting in a reluctance to dismiss workers even in crisis situations.

- SMEs are often very strongly embedded in their local environment. In the framework of restructuring this, on the one hand, becomes important in terms of interrelationships between local firms and knock-on effects of one (large) firm in restructuring on its local suppliers and business partners. On the other hand, there often exist personal/social ties of the owner/manager within the local community which also composes the firm’s workforce. This also fosters socially responsible behavior in case of restructuring projects.

Having in mind characteristics of strategic crisis as well as restructuring projects specifics of SMEs we are proposing a two-dimensional conceptual framework consisting of systemic and processing dimension for mastering restructuring projects in strategic crisis situations.

**SYSTEMIC AND PROCESSING DIMENSION FOR MASTERING RESTRUCTURING PROJECTS IN STRATEGIC CRISIS SITUATIONS**

Mastering strategic crisis solves the complex problem of managing strategically relevant changes that are occurring in the business environment. It requires the most comprehensive integration of multiple theoretical and practical areas. When designing a model of mastering strategic crisis in SMEs we are not focusing on finding solutions to address particular strategic crises cases, but to establish a system for mastering strategic crisis with restructuring projects.

The definition of certain key elements and the links between these elements for the model of mastering strategic crises derive from the most common causes of a strategic crisis. The focus is primarily on objective reasons. We consciously leave subjective reasons on aside, as for solving those issues completely other measures are necessary that do not go directly into the context of the model we are developing and presenting here. Furthermore, the model is based on conditions that need to be fulfilled:

- Holistic, i.e. a systems approach to mastering changes and strategic crises at all organizational hierarchical levels and in all parts/units of companies that are involved in this processes;
- Integration and understanding of the interdependence between all entities and actions that arise in the restructuring processes;
- Operational orientation of restructuring projects and programs;
- Creativity, inventiveness and innovativeness of all actors involved in the process of project oriented restructuring.

Figure 1. Basic two-dimensional model of mastering strategic crisis with restructuring projects
Based on those starting-points we propose a basic two-dimensional model of mastering strategic crisis with restructuring projects, which basically involves two aspects (Figure 1). The **process aspect** of mastering restructuring projects and their connection with regular or continuous business operations (the process of mastering restructuring projects is further divided into three sub-processes, namely sub-process of strategic and project treatment of changes, sub-process of creating necessary restructuring projects and programs and sub-process of implementing restructuring projects/programs). The **system aspect** of managing restructuring projects defines the requirements to be satisfied by the company as a whole to achieve desirable effects from those projects (an appropriate organizational and project maturity; consideration of the requisite and sufficient interdependencies between changes that occur in the firm’s environment, and projects/programs company is using to respond to those changes; consideration of the necessary creativity, inventiveness and innovativeness of management and other employees of the company).

**Process aspect of mastering restructuring projects**
Mastering processes in restructuring projects starts with sub-process of strategic and project treatment of changes, beginning with change detection and analyzing whether change potentially have impact on the emergence of strategic crisis in the company. In the second sub-process – designing projects and responses to changes, if necessary, firm’s strategy is supplemented or transformed. Depending on the availability of resources (time, financial resources, equipment and staff, relationships with network partners, etc.) first strategic portfolio of projects and restructuring programs shall be made, while less complex measures are included in the firm’s annual operational plans. In the third sub-process – realization of restructuring projects, those are holistically prepared, followed by composing the second (final) strategic portfolio of restructuring projects, following by the start-up of their implementation. During the implementation of projects a strategic and project controlling needs to be assured; its purpose is to monitor the implementation of projects and in particular to estimate the accordace of the results achieved with intended objectives and strategic intentions. At the end of the projects their formal completion is following, which means documenting the transfer of projects’ results, the formal startup of the exploitation and beginning of the regular business operations. With the preparation of final reports and archiving of project documentation the process is concluded.

**System aspect of mastering restructuring projects – organizational changes**
The extent of changing business environment increasingly transcends individual’s capacity to monitor and perceive the influence of changes. Therefore, for these issues formal or informal cooperation of various actors from different key disciplines, which mutually inform and highlight the changes and their potential consequences to each other, should be provided. These actors are beside company’s owner/manager also their employees and especially professional staff, partners, members of business networks, etc.. Along with this regard the establishment of appropriate organization, to provide adequate support for the implementation of restructuring projects, is rather difficult challenge.

**System aspect of mastering restructuring projects - holism and interdependence**
Considering the requisite holism and interdependence in defined sub-processes we are achieving appropriate holism, consideration and consistency of all effects arising from adjusted and redefined strategies. Better portfolio of restructuring projects is enabled, as individual projects in the portfolio are treated as a whole. An impact assessment of projects in this case is not only focused on internal and possibly on the external business environment, but also on the social environment or the entire ecosystem. The logic of the requisite holism and interdependence must be followed also during the implementing strategic and project controlling.

**System aspect of mastering restructuring projects - creativity and innovation**
The successful implementation of restructuring projects largely depends on the creativity, inventiveness and innovativeness of actors involved in the projects. Already in the sub-process of mastering changes the company performs much better, if it is innovative in setting up and changing modes of changes perception. Creativity is also needed during the transformation or complementing company’s strategy in a way that they define unique strategic guidelines and take advantage of the changes detected in the environment. However, even the most unique strategies will not be implemented successfully if we do
CONCLUSION
Slovenia has undergone three fundamental restructurings in the last 20 years: the first was the transition to an independent country; the second was the transition from a socialist to a market economy; and, the third was joining the EU and Eurozone. SBA Fact sheets 2010/2011 show that Slovenia’s SME sector closely resembles the EU’s. Unfinished transitional process, and relatively poor main economic indicators compared to EU are reasons why Slovenian firms facing considerable challenges in managing their restructuring projects in crisis situations. According to the European Restructuring Monitor (ERM) we are describing different types of SME restructuring, such as: relocation, outsourcing, offshoring/delocalization, bankruptcy/closure, merger/acquisition, internal restructuring and business expansion. Deriving from some typical elements SMEs are facing in restructuring projects we are proposing two-dimensional model combined of process and system aspect for mastering strategic crises with restructuring projects of SMEs.

Unfortunately, economic policy measures in a small, open economy like Slovenia are limited. Since the future is very uncertain and further deterioration of economic conditions is expected, economic policy must focus on at least three basic areas: i) reduction of uncertainty in the business environment; ii) strengthening the basic social network; and iii) preservation of future fiscal power (Bole, 2009). In every economic crisis, the labor market is affected the most. Therefore, one of the most important policy challenges is how to design and implement measures that are, at the same time, socially sensitive and economically effective.

Restructuring projects call for different micro-level solutions to be successful in SMEs. The proposed two-dimensional model emphasizes the need for a holistic perception of reality - perception and interpretation of changes and the design and implementation of restructuring projects, taking into account the different subjective positions of stakeholders, such as SME’s owner/manager, employees, business partners and networks. In restructuring projects, this requires complex analysis of the interrelations between them, understanding the positive and negative synergies that occur between individual components of the system, non-linear perception of reality and analyzing numerous feedbacks.

REFERENCES
ERM: European Restructuring Monitor. [www.eurofound.europa.eu/emcc/erm]


