THE TURNAROUND OF SOUTH AFRICAN AIRWAYS: 1998 - 2000

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We certify that this report is our own work and all references used are accurately reported.

Signed:

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ABSTRACT

South African Airways (SAA) experienced a period of sharp decline in the years 1995 to 1998. This led to the appointment of a new CEO and management team to turn the airline around. A strategy was implemented focussing on improved customer service, improved revenue management, cost reductions, the formation of a global network of alliances, the upgrade and standardisation of the fleet, transformation of staff and the introduction of a new first and business class product. The airline was successfully turned around within a period of two years and is currently in the phase of consolidating this success.

The case study explores the period of decline before focussing on the sequence of key action steps that the new management implemented in turning the airline around. It provides students and managers with a practical example of the turnaround process, and assists them in linking turnaround theory to practice.

Keywords: Turnaround, Decline, Strategy Implementation, Customer Service, Alliances, Fleet, Turnaround Expert, Strategic Leadership, Performance Measurement, Global and South African Airline Industry, Strategic Focus.

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THE TURNAROUND OF SOUTH AFRICAN AIRWAYS 1998 - 2000

Introduction

In June 2000, Coleman Andrews, the Chief Executive Officer (CEO) of South African Airways (SAA), announced that the airline had achieved an operating profit of R557 million (US$1=R6.89 at the time) in the 1999 financial year. This was a swing of almost R700 million from the previous year's operating losses of R130 million.

This announcement was made on the second anniversary of Andrews' appointment as CEO. He attributed the swing to a wide ranging cost cutting exercise and a stronger focus on revenues. He was pleased that within a period of just two years, he and his team had managed to turn the airline around. Another great highlight of the year had been the sale of a 20% stake of the airline to the SAirGroup, the parent company of Swissair. This sale was part of the South African Government's drive to privatise state assets.

The drastic steps taken to turn the airline around had resulted in many tensions within the organisation. He felt that his focus for the next two years of his four year contract would need to be on people and service, following the difficult period of taking the country's national carrier out of its near fatal nose dive. He commented that

"the theme in the first few months was to stop the bleeding, and then to strengthen the mind and body. Now we are building the soul". [10]

Crude oil prices had increased from around $10 per barrel at the beginning of 1999 to around $30 per barrel in June 2000 (See Figure 5 for Brent Oil Spot Oil Prices), causing great uncertainty for airline companies such as SAA, where fuel is the major cost driver. SAA had found it difficult in the increasingly competitive environment to pass the oil price increases on to consumers. While SAA had made major gains in terms of improving customer service, domestic and international passengers still complained that the service was below that of international standards.

There had also been speculation in the media that Andrews intended resigning before the end of his contract. He was quick to dispel the rumours and remained confident that he had the backing of the key stakeholders and that he would serve out the remainder of his term. He felt that he had started something that he not yet finished. Having pulled the airline out of financial distress, his ambition was to set SAA on the road to becoming one of the world's top five carriers within the next two years. This would coincide with the South African Government's plans to take the airline to an Initial Public Offering (IPO) by then. Clearly, there were many challenges that lay ahead for the airline.

History of SAA

On 1st February 1934, the Union of South Africa acquired all the assets and liabilities of a private airline, Union Airways, and absorbed it into a new national airline - South African Airways. The airline started with two Gypsy Moths, a Puss Moth, three Junkers F13's and a Junkers W34; with chartered and scheduled flights between Cape Town, Durban and Johannesburg (three major South African cities). The inaugural flight of the three Junkers, to Durban in late 1934, caused a near riot. Crowds gasped in amazement at what was then considered the enormous size of these aircraft.

New routes into Africa were pioneered, as far afield as Kenya. The first international service to Bournemouth in the United Kingdom (UK) started in 1945 and in October 1960, SAA began flying Boeing 707's to the UK and Europe. The first non-stop flight to Europe followed in 1962, and in August 1963 a new route to Europe was pioneered along the west coast of Africa. In 1973, the airline initiated another direct link between South Africa and the Far East; this weekly flight to Hong Kong was followed by a flight to Taiwan in 1980. SAA suffered what was possibly its worst disaster in 1987 when the 'Helderberg' crashed into the Indian Ocean; all 159 passengers and crew were killed and the cause of the crash was never determined.

A milestone was reached in 1989 when SAA transported over 5 million passengers in one year, for the first time. The year 1990 marked the beginning of the return of South Africa into the global community of nations, after more than 30 years of political, economic and social isolation (See Exhibit 1 for an explanation of apartheid). In April 1990, SAA became a division of Transnet, the South African state-owned transport services corporation (See Exhibit 1 for a profile of Transnet). This was the beginning of a process of forming the airline into a fully market-related commercial enterprise. During the early 1990's, the National Party Government under De Klerk, moved towards a liberal transport policy and a privatised state, as a reflection of both their political interests (anticipation of a loss of power to the ANC) and of international norms. At this time, the National Party made the first attempts to privatise SAA, but met with considerable resistance from the ANC who feared that this represented a sale of a valuable national asset.

SAA had traditionally been insular in its outlook towards the global market. After the lifting of sanctions and other restrictions previously preventing SAA landing rights in many countries, the opportunity presented itself for SAA to expand its flights to international markets. SAA introduced three weekly flights to New York in November 1991. The first SAA Airbus arrived in Johannesburg that same month, after completing the first flight over Angola since 1975. In January 1992, flights to Perth and Sydney were resumed. Weekly flights to Luanda began and the number of other African destinations increased. In June 1992, a joint agreement between SAA and Air Afrique introduced twice weekly flights between South Africa and West and Central Africa. At the same time, services to Bangkok and Singapore commenced, followed by the first scheduled flight to Munich in August. A direct flight between Cape Town and Miami started in December 1992. Larnaca, Cyprus was included on the Tel Aviv route from February 1993, and Hamburg was introduced in June. During 1994, Sao Paulo was added, and Dusseldorf replaced Hamburg as the third destination within Germany. In the same year, additional services to Victoria Falls and Miami, as well as a direct flight from Cape Town to Hong Kong came into operation. In July 1995, Alliance Air was launched to service direct flights between Dar es Salaam, Entebbe and London, with SAA holding a 40% share. At the end of 1995, Buenos Aires was also added to the network. In a period of 60 years, SAA had extended its operations to include daily flights between major South African cities and its route structure to include five Continents.

The Global Airline Industry

For nearly 40 years, after the end of the Second World War, the structure of the airline industry remained largely unchanged. This was mainly due to the strategic importance that governments attached to aviation as a mode of transport and the regulations they imposed on the industry.

Since the 1970's, air travel grew as a result of the falling real price of air transport and the growth in personal income. The international air transport industry in the 1980's and 1990's was characterised by high growth, deregulation, low profitability, alliances and mergers. Industry growth averaged 11% per annum between 1960 and 1989, but declined during the

1990's. The economic crisis in Asia further depressed growth, because of the price sensitivity of the industry and also its exposure to exchange rate fluctuations (See Figure 12 for share price performance of selected airlines).

The emergence of dominant operators in the industry had been limited by the number of airlines, government aid to ailing state-owned enterprises, and the efficiency gains of 'hub-and-spoke' systems, where hubs were often based in the home country of the airline. The industry had therefore been highly competitive and highly price sensitive. The high capital intensive nature of the industry exposed airlines to high financing costs, and this further limited the emergence of dominant operators. According to the International Air Transport Association (IATA), scheduled airlines had turnover close to 1% of the world GDP (US$280 billion) in 1997. Margins were low, however, with combined net profit of around US$4 billion. In the last 35 years, the air transport industry has experienced only two periods of sustained profitability; 1963 to 1968 and 1987 to 1989.

The high degree of international regulation and the highly competitive nature of the industry made it difficult for airlines to become bigger than what their national economy and industry structure allowed. In response to low profitability, high competition, and deregulation, the industry has since the late 1980's been characterised by the formation of strategic partnerships, alliances or mergers. Ten years after the deregulation of US carriers began in 1978, the three largest airlines accounted for 86% of the industry operating profit. Mergers and acquisitions achieved economies of scale. However, as equity mergers were tightly controlled, airlines embarked on code-sharing agreements through contractual mergers. This helped them to market their services jointly, to purchase jointly thus achieving benefits of increased purchasing power, and to increase market reach through the operation of a network of airlines.

European airlines followed the US example, seeking to achieve dominance in their home markets, expand into other regional markets, and form strategic alliances to assist in achieving these goals (See Figure 11 for the major global alliances). A number of changes in product pricing and operational structures ensued. Cost cutting exercises were implemented in which labour costs were reduced through a reduction in staff numbers, a re-negotiation of staff contracts or, a relocation of activities to countries where labour costs were not as high.

The European Community Committee on Aviation Deregulation encouraged governments to privatise their airlines in order to reduce the subsidisation of air transport services. British Airways was privatised in the late 1980's, and generally showed positive returns in the years that followed, which was a notable achievement in the competitive and volatile airline industry. Following British Airways, a number of international airlines sought to gain from the experience and capital that was frequently brought to bear when other international airlines invested in them. The late 1990's thus witnessed the partial privatisation, through the sale of equity, of a number of national airlines in both the developing and developed world.

In 2000, the major airline global players, in terms of market share, included British Airways, Delta Air Lines, Continental, Air France and Lufthansa (See Figure 13 for the global market shares of selected airlines).

The South African Airline Industry

The deregulation of the global airline industry in the 1970's and 1980's had a lasting impact on the shape of the industry as new players could enter the market and compete with established players, and in most instances this led to intense price competition. The South African airline industry went through a similar experience when the domestic industry was deregulated in 1990. The domestic carrier, SAA had been a protected monopoly since the 1952 National Transport Commission Policy that guaranteed the ongoing monopoly of SAA. However, in 1990 the Air Service Licensing Act effectively deregulated the industry by removing protection for license holders for domestic routes and this dropped the primary barrier of entry into the industry and opened the way for several new competitors to enter the market.

The early and mid 1990's were turbulent times for the South African airline industry as deregulation was ushered in. In 1990, SAA's market share of the domestic market was 95%, but by 1992 Comair and Flitestar, both new entrants in the domestic market, had captured 7% and 22% respectively of the lucrative Johannesburg - Cape Town route. (See Figure 1 for SAA's domestic market share between 1990 and 1998). By 1994, Flitestar had ceased operations and Sun Air, the airline inherited by the South African Government from the former Boputhatswana Government (a homeland in the old apartheid South Africa) and Phoenix Airways had entered the domestic market. Phoenix was not successful and ceased operations after less than a year. In 1995, Nationwide entered the domestic market and by then SAA's share of the domestic market had dropped to 73%.

The mid 1990's saw a host of alliances being formed between domestic operators and international carriers in an attempt to capture the massive growth of the overseas tourism market. Sun Air formed an alliance with Virgin Atlantic and KLM, Nationwide with Sabena, Comair with British Airways, and SAA with Lufthansa and American Airlines.

In August 1995, SAA CEO Mike Myburgh and Comair Chairman Dave Novick, lobbied the Government for legislation to protect passengers. They wanted the public protected against new entrants who were undercapitalised and did not have the requisite expertise, and were concerned that aviation in South Africa seemed to be following the international trend where only one in every ten new airlines survives. In November 1997, the South African Government privatised Sun Air. SAA's domestic market share had fallen to 54% by 1998, with the rest being shared by Sun Air, Comair and Nationwide.

SAA Period of Decline: 1995-1998

Mike Myburgh was promoted to the position of CEO in 1993. He led the organisation through some of the most turbulent years in the political history of the country and that of the local airline industry. He faced the challenge of responding to increased domestic and international competition and steered the organisation through the critical period of the political transition. Despite the increased competition on domestic and international routes, SAA reported profits in 1994 and 1995 (See Table 1 for a summary of the financial performance from 1991 to 2000). This was mainly because of increased demand on international routes, and the growth of the domestic market as the country recovered from the economic recession of the early 1990's (See Figure 7 for GDP growth/decline 1990-2000). In August 1995, Myburgh commented:

"We have to form alliances. We are too small to be solely international and too big just for the national scene". [14]

The years 1995 - 1996

By 1995, SAA had developed into the largest commercial airline operating in the African continent and was rated among the 50 largest airlines in the world. During 1995, the strategic focus under Myburgh's leadership was on building alliances and route networks. SAA signed an agreement with Lufthansa to improve customer and passenger service through code-share flights (See Exhibit 1 for an explanation of 'code-share'), the interlinking of the airlines' respective frequent flyer programmes and joint cargo operations.

Several improvements were made to SAA's fleet of aircraft to enhance its image. These included a smaller first class cabin, a larger business class configuration, improved seat pitches in all three classes and a standardised appearance in all Boeing 747 aircraft. A significant aircraft acquisition programme of Boeing 777's was announced, to meet increased demand from international passengers arising out of the reintegration of South Africa into the global community and the consequent increase in tourism. SAA acquired two used Boeing 747-300 aircraft on the open market. In addition, two Boeing B737 aircraft and one Boeing 747-200 combi aircraft were converted to freighters.

To keep up with unprecedented growth of 22% in 1993/94, and 20% in 1994/95, SAA Cargo expanded its operating fleet as well as its warehouses in Johannesburg, Cape Town and Durban. After the signing of the agreement between SAA and Lufthansa, SAA Cargo began serving the Johannesburg - Nairobi - Frankfurt route with a Boeing 747-200 freighter, increasing the joint cargo services from two to four per week.

Negotiations with unions with regard to employment conditions were successful and agreement was reached with labour unions for greater flexibility in the introduction of shiftwork in day shift areas and the use of craftsmen in lesser skilled functions.

The SAA Cadet Pilot Training Programme was originally implemented in 1994 with the aim of helping previously disadvantaged young South Africans become airline pilots. The programme was fully sponsored by SAA and the new intakes were first sent to Adelaide in Australia for 18 months of flight training. The airlines's third intake of Cadet Pilots commenced training during the year. SAA aimed to train 40 pilots a year until the year 2000. By promoting and making careers accessible to previously disadvantaged South Africans, SAA aimed to attract and retain the best from all the population groups in South Africa.

Uncertainty about the future

Myburgh was concerned that SAA was still too vulnerable to political interference. Privatisation would create a distance between SAA and the Government, which would allow the executive management team the freedom to make strategic and operational decisions. Transnet and the executive management team saw profitability and a strategic capability that would enable SAA to compete in the international arena, as key issues for the future. The leadership of SAA felt temporarily paralysed while the new Government reviewed the primary objectives of the organisation. A clear political directive for privatisation only emerged in 1996.

Increased domestic competition

In 1996, SAA had 63% of domestic market share, but with growing competition from new players and a dismal track record, it was losing three percentage points a month of market share. SAA was uncompetitive on price, typically 12% to 25% higher than its competitors. International isolation and Government protection had separated the airline from the practice of using international benchmarks to improve performance and management practices. Employees at SAA were thus isolated, with limited exposure to the kind of service expected by customers who had the option of a variety of international airlines. The airline suffered from a lack of concern about market orientation and poor service quality. The perception of employees within SAA regarding the level of service quality differed from the perceptions of passengers and other outsiders.

SAA was facing financial losses by June 1996 when they launched a R15 million promotion in an aggressive marketing war against domestic competitors Comair and Sun Air. In addition to the increased market shares of Comair (20% from 15%) and Sun Air (17% from 10%), SAA found itself under threat from the recent alliances formed between Comair and British Airways, and Sun Air and Virgin Atlantic. In November 1996, SAA offered discounts of up to 60% on the price of 12,000 seats on domestic flights. In December, it offered discounts of 55% on 20,000 seats on domestic flights. The competitors responded by matching SAA's price cuts.

SAA experiences losses

For the period April 1996 to March 1997 SAA reported a net loss of R323 million (See Table 1). Transnet Managing Director (MD), Saki Macozoma, attributed the losses to the decline in the value of the Rand in mid-1996 and the consequent increase in all costs that were dollar denominated (See Figure 6 which gives the US$/SA Rand exchange rate between1994 and 2000). The increase in fuel costs exacerbated the situation. Also the increase in the number of foreign airlines operating into South Africa resulted in over capacity being offered on many routes. Coupled with increased competition in the domestic market, these factors had a negative impact on SAA's profitability.

The history of Government involvement in SAA had been such that the impact of operating losses was not felt anywhere in the organisation. At the executive level, the focus tended to be on capital structure and gearing in relation to the operational capacity of the airline, such as the potential to acquire new aircraft. As long as the airline was under Government ownership there was no threat of financial failure.

Passenger numbers increased by only 1% between 1995/96 and 1996/97, and revenue from passengers increased by 13.5% (See Table 1). In terms of cargo, tonnage carried increased by 5.7% and revenue increased by 17% to R910 million. The depreciation of the Rand helped to boost trading in the international cargo division as exports rose. Management identified better preparation to the volatility of variables such as currency fluctuations and the elimination of additional fuel costs as important actions to keep operating costs under control.

African and international expansion

Continuing in its drive to expand into Africa, during 1996, SAA introduced new routes to Ghana and Ivory Coast, which brought the total number of destinations in Africa to fifteen. On the international front, additional services were introduced to Mumbai, Miami and New York, and Bangkok was developed as a primary hub in Asia. SAA's and American Airlines' existing co-operative services agreement was extended to include additional reciprocal code-sharing services between Johannesburg and Cape Town and several points within the USA. The airline developed a new first class product aimed at improving the standard of onboard service.

The years 1997 - 1998

SAA not ready for privatisation

In February 1997, the South African Government announced that it wished to speed up the partial privatisation of SAA and a decision was made to sell a 30% stake to a foreign partner. Although speculation in the industry that SAA's privatisation was imminent, Transnet's Chairman Louise Tager stated that SAA was not ready for privatisation or an equity partner. SAA was still a division of Transnet and before the Government would be able to sell shares in it, the corporate structure would have to be transformed. Also, against a backdrop of losses, the Government had not completed an evaluation of the airline, nor had it made a firm decision on what percentage it wished to sell. There was consensus that SAA would need to trade its way out of its loss situation before privatisation plans could gain momentum.

SAA launches new corporate identity as price wars escalate

In March 1997, SAA unveiled their new corporate identity in Johannesburg. Three years after the birth of the new South Africa, the airline shed its old corporate colours that reflected the old South African flag and adopted the colours of the new South African flag. Along with the new corporate colours, SAA announced a new vision, mission and values for the organisation (See Exhibit 2 for SAA's values):

SAA Vision

"We will fly the spirit of South Africa to the world and be a role model to all people. We embody the magic of free South Africa to host a safe, warm African experience."

SAA Mission

"South African Airways is committed to being a dynamic, efficient and safe airline, caring for its employees, providing warm, personal service for its clients, the realisation of profits for its shareholders and contributing to the wider community."[35]

In the domestic market, price wars escalated with SAA offering a 65% discount on all domestic flights between April and June 1997. SAA also tried to counter the increased competition on the Johannesburg - London route from Virgin Atlantic and British Airways.

Employee morale

The losses during 1996/97 and the announcement of the partial privatisation caused considerable uncertainty amongst employees. Although some employees supported and liked Myburgh's leadership style, employees generally felt that the executive management team was unable to offer clear vision and direction to the middle management of the organisation. SAA suffered the disadvantage of having emerged from being a state owned enterprise and had thus adopted the corresponding bureaucratic planning processes. The organisation had a hierarchical top-down structure with very little interaction between divisions, and there was a lack of cohesion in the senior management which had resulted from a period in which managers had built 'empires' within SAA.

SAA had a history of co-operation with well organised unions. As a result SAA salaries were competitive compared to other international carriers. Wages are the second highest cost driver in the airline industry and thus play a key role in cost control. Myburgh had introduced change initiatives and created structures to facilitate change, but employees felt that the initiatives lacked penetration and were not well co-ordinated. The unions did not actively resist change as long as they were adequately involved in the process determining the outcomes of the change. Although there was a high degree of loyalty among the staff, there was the emergence of factions amongst employees. Some of these factions occurred within groups at different levels within the organisation and there was also an underlying racial dimension to the emergence of these factions.

International expansion continues

During 1997, SAA concluded a code-share agreement with Thai International Airways and Japan Airlines. On the international front, SAA also effected major changes to its operations to and from continental Europe, in order to prevent becoming marginalised in the major traffic producing countries through frequency increases by its competitors. Furthermore, it acted in such a way as to capitalise on opportunities in new uncontested markets that had shown significant growth over the past few years.

Disagreement between Nomvete and Myburgh

Myburgh felt that SAA did not have enough planes and believed that Chairman Nomvete's decision to delay the delivery of two Boeing 747-400's that were due to have been delivered in October 1997 had resulted in a loss of traffic to competitors. It was estimated that a single 747 generated earnings of R20 to R30 million a month. The aircraft would now only be delivered in July and October 1998.

SAA's decline worsens

For the period April 1997 to March 1998, SAA reported a loss of R244 million, which was more than 10 times the loss reported in 1993 (See Figure 3 for a graphic representation). Revenue during the year increased by 16% year on year, while passengers decreased by 2%. Yields increased by 16% and capacity increased by 2.7%. Cargo had another successful year, reporting a new turnover record of R957 million and an increased contribution of R302 million to SAA's profits. The regional operations into Africa, the Indian Ocean Islands and the Middle East were profitable during the year. On these routes, passengers increased by 10% year on year, while revenue increased by 23%. Jet fuel procurement costs were 4% below budget at R1.196 billion. SAA enjoyed lower international fuel prices which, on average, were 15.6% lower than those in 1996/97. Total expenditure on jet fuel increased by 1.18%. 'Operation Clean-up', a cost cutting programme during the year saved the airline R203 million, but all this was not enough to prevent the losses.

The 'open skies' policy also created intense competition for SAA. The number of airlines operating into South Africa increased from about 21 in 1990 to about 60 in 1997. On a technical level, SAA had difficulty competing with international carriers whose aircraft were significantly younger than their own. On the other hand, isolation from the international community had had the effect of causing SAA to develop extensive training and technical capacity. A large percentage of other airline's maintenance work was undertaken by SAA in order to absorb spare capacity.

By May 1998, SAA was being faced by mounting losses, was riven by racial tensions and crying out for a coherent business strategy. Zukeli Nomvete resigned as Executive Director and was replaced by Mafika Mkwanazi, Deputy MD of the holding company Transnet. Mkwanazi faced two major tasks; to return SAA to profitability and mend relationships among divided and demoralised managers.

Under Nomvete's stewardship a number of senior managers had left the organisation. The resignations reflected a deeper malaise, and there was friction between Myburgh and Nomvete. Lower down the line, tensions between senior managers were rife and morale was very low. SAA middle management represented an 'old guard' who lacked foresight, vision and focus. They resisted transformation in SAA and this had a negative impact on operations. Senior executives in SAA had often been appointed from positions in the railways, the dominant arm of Transnet's operations and thus had no international experience common to managers in other international airlines. The management mentality, which had been prevalent in the organisation since the 1960's, focused on generating profits through controlling costs rather than by focussing on strategic alignment and positioning within the industry. These conditions were made worse by an atmosphere of paralysis; decision making had ground to a halt.

Appointment of Coleman Andrews: June 1998

The worsening situation at SAA prompted the Transnet Board of Directors to search world-wide for a CEO who could rescue the organisation. In June 1998, Saki Macozoma, Chairman of Transnet, announced the appointment of Coleman Andrews as CEO of SAA. Andrews was regarded as an expert in the airline environment and in corporate revenue management, and his contract with SAA was to last for three years, renewable for one year thereafter.

Andrews' appointment was made against the background of continued losses being suffered at SAA. When Andrews arrived, SAA was heading for their worst losses ever, expected to be between R500 and R550 million for the 1998/1999 financial year. With the impending privatisation of South African Airways, it was clear that Andrews had a challenging task ahead.

The Transnet Board had no qualms about Andrews's ability to take the airline successfully into the new millennium. Said Macozoma:

"We searched the world to find the right man for the job, and we have found him. Coleman is a professional with an enviable track record and exactly the right qualities needed to equip SAA to become a profitable and competitive airline. By having him at the helm we will add value to the airline, improve customer service and benefit our country as a whole".[35]

Background of Coleman Andrews

Coleman Andrews, aged 43, at the time of his appointment, graduated with a BA magna cum laude from Dartmouth College, New Hampshire, in 1976. He was by then already attached to Gerald Ford's White House as a staff assistant for economic affairs, preparing briefing papers for the President, the Cabinet and the Economic Policy Board. In 1978, he joined Bain & Co, in Menlo Park California, a firm of consulting specialists with extensive experience in airline turnarounds. In 1979, he completed his MBA at Stanford University, graduating in the top 10%. He co-founded Bain Capital in 1983, one of the US's most successful venture capital funds.

In 1986, he was recruited to lead the turnaround of World Airways, where he served until 1993 as CEO. He was regarded as being fanatical in the disciplines of cost and revenue. World Airways provides worldwide passenger and cargo air transportation under contracts with major international airlines, the U.S. Air Force and international tour operators with a fleet of MD-11 and DC10-30 aircraft. He turned the airline from an accumulated loss of US200 million (R1.1 billion) to an after-tax profit of US70 million (R385 million) and continued as Chairman of the Board of World Airways until 1998.

Andrews was not just the former boss of a revived, albeit small airline, but also an influential businessman and social commentator with strong religious convictions. He was regarded as a social and political conservative having stood for the position of Lieutenant-Governor in his home state of Virginia on a Republican ticket in 1999. A pilot himself, he flew aircraft from the Cessna 150 to the Airbus 340. He was a keen animal and nature lover as well as a breeder and trainer of labrador hunting dogs. Andrews also loved riding quarterhorses in amateur rodeos.

Diagnosis: June to July 1998

When Coleman Andrews arrived at SAA in June 1998, business conditions were described as very fragile. He had been given a free reign by Macozoma to choose his own management team. His first action was to appoint a new leadership team for the organisation and apart from 2 of the top officers all the rest were replaced (See Figure 8 for SAA's Top Management Structure during the Myburgh era). Andrews recruited his new management team by promoting managers from within the ranks of the organisation as well by recruiting experts from within South Africa and globally. He poached David James from Virgin Atlantic to head up global sales. Three of the Executive Vice Presidents were Americans, Bill Meaney, Don Garvett, and Kevin Wilson. Don Garvett had been a consultant to 60 airlines, a University Professor and a Vice President at Pan Am and Air Florida. He was appointed to head up the Commercial and Planning Division. The new team was also more diverse, with 5 black appointments, 2 of whom were women (See Figure 9 for Andrews' leadership team).

During his first 6 weeks at SAA, Coleman Andrews and his newly appointed team put together a diagnosis of the airline's illnesses. On his first day at Airways Park, SAA's headquarters, Andrews wandered around unescorted stopping to talk to people. He encountered employees uncertain about their company's future and their jobs. He believed that it was important to spend at least 45 minutes a day talking to staff and by the end of the first six weeks, he had met about 6 300 of the airline's 10 850 employees, 70% of whom had never seen their CEO before. He found that SAA lacked a clear, cogent, positive and powerful vision of how to win in international aviation circles. SAA employees desperately needed a clear and compelling vision of what their future could be, and clarity was necessary in order to get employees to embrace the vision and work towards its accomplishment.

Andrews' immediate aim was to oversee the revitalisation of SAA. The goal was to make the airline customer driven. He was passionate about keeping close contact with customers, finding new passengers and regaining those lost to the airline. This entailed listening carefully to the customers, to what they want and what they were willing to pay for and in this regard, customer service topped the list. Since the airline was getting at least four or five negative articles in the press for every positive one it was necessary to analyse the root causes.

Customer surveys were conducted, which found that customer perceptions of SAA were that they were a bloated, uncaring, arrogant, self-absorbed parastatal. The public perceptions were exceptionally negative; they felt that the product was bad, and that SAA would never fix it. Compared to their two major domestic competitors, SAA was rated as materially lower on the most important service measures, even though its prices were higher than its competitors. The customers' biggest complaint was that SAA flights were always late. Andrews and his management team identified the performance of the business section, in particular, over the previous 15 to 16 months, as a problem area and given that 80% of SAA's passengers were business passengers this was considered unacceptable.

Marketing efforts were found to be uncoordinated. The various departments of SAA were each pursuing their own strategy of how to market the company or the product. The management team pasted all the existing marketing material up on a wall one day and realised that there was no common theme running through them. There was at this stage no compelling reason to spend millions encouraging travellers to try a product that was likely to disappoint them and nor was there reason to persuade them that the product was really better than their adverse perceptions. SAA would need to first improve service levels before undertaking major marketing campaigns.

Costs had been spiralling out of control for the past few years and in order to turn the airline around, the management team would have to attack every element of cost and revenue. The airline's cost structure was reviewed in order to bring it in line with that of its major competitors and this included a complete assessment of the airline's routes, to eliminate those that were not viable and increase the frequencies of those that were.

The current Management Information Systems were found to be inadequate for decision-making, and better cost and revenue management. The need was identified to acquire top-of-the-range hardware and software. Andrews believed data and analysis to be a priority:

"When big decisions have to be made, they should be based on the best available information. You can't do the job if you don't have the right tools".[5]

Furthermore, operationally, SAA suffered from high domestic costs and low crew production levels. Service levels were uneven and inconsistent. On an organisation and culture level, Andrews and his team detected a bias towards inaction and where problems had been identified these rarely went beyond being discussed in meetings. Seldom innovative, SAA's nature was defensive, typically responding to competitors. Inward-focused, SAA compared itself against itself, rather than against the best. The culture of the organisation seemed to be that it was built to serve employees, off-loading passengers to make space for staff and their families. Pockets of corruption were also detected within the organisation, ranging from attendants walking off flights with costly items to contracts being awarded to employees' family and friends. What was working well at SAA was the performance of the entire flight deck and cockpit crews, who were ranked among the very best in Asia, Europe or the United States. The airline also had a high technical proficiency although costs in this area were too high.

The new team identified a need for SAA to revitalise its fleet. Andrews believed in aircraft commonality, type and size. Part of his strategy was that he wanted to see drastic reductions in engine types and more uniform cabin configuration. SAA currently had three different aircraft types with different makes of engines and configurations, all serving the domestic market. One of the issues facing the new team was whether to reactivate the stalled, controversial Boeing 777 order, which had cost SAA around $60 million in deposits. The Asian economic crisis of 1998 had a dramatic impact on global markets and resulted in many aircraft orders being cancelled but this presented the airline with opportunities to negotiate better deals. There was also the option of leasing aircraft rather than outright purchase, which had previously been the trend.

The South African Government and Transnet had set a deadline of October 1998 for the partial privatisation of SAA. Andrews was not concerned about the deadline and was more concerned about performance. He believed it was far more important to get the airline back to profitability so that talks with foreign equity partners could be held from a position of strength. While many analysts believed that the major advantages that a foreign partner would bring to SAA were cash and expertise, Andrews was more interested in a partnership that would increase SAA's distribution power and would improve SAA's ability to execute its strategy.

The new team reviewed the current alliances that SAA had in place and, linked to the issue of privatisation, it was imperative that SAA enter into alliances with one of the chief airlines. Consequently, the search for partners would have to begin shortly.

Two aspects of government policy were identified as hampering SAA's development. One of these was a ban on transporting domestic passengers on the domestic legs of international flights. This included the everyday operation of 747 aircraft between Johannesburg and Cape Town - on either the start or finish leg of their international flights - with about 70 to 80 percent of their seats empty. Another major problem was the price at which SAA had to buy its fuel, which was dramatically above market rates, and this amounted to a penalty of about R80 million a year.

At the end of the six-week period, after having diagnosed the 'illnesses' of the airline, Andrews announced a three-phase plan to return the aircraft to profitability and position it to be one of the five top airlines in the world. The first phase would be to 'stop the bleeding', the second phase to 'strengthen the mind and body', and the third phase to 'develop the heart and soul'.

Stop the Bleeding: August 1998 to April 1999

Andrews and his leadership team set as their aims rectifying the problems of the past and moving SAA into the top ranks of the airline industry. The vision and mission statements that were developed during the Myburgh era were not altered, but, in addition, SAA required a clear set of achievable goals and a concise and effective game plan. The 'Strategy for Winning' was thus developed as an implementation action plan. It called for the simultaneous and sustainable execution of the following seven pillars:

- Focussed cost reduction programmes
- Improved revenue management
- Expansion and development of powerful alliances aimed at creating a highly profitable network
- Sharply improved customer service
- Fleet upgrades and standardisation
- Transformation of SAA staff
- New first class and business class product

The 'Strategy for Winning' became the primary focus of all corporate communication. While the existing vision and mission were maintained, the 'Strategy for Winning' was the tool to mobilise staff within the organisation and to communicate with external stakeholders such as Transnet, the South African Government, customers and the public at large.

Customer Service

The first area of focus was that of improving customer service. Having found that late flights were the most common complaint of customers, SAA engaged its entire employee group in a simple but powerful scheme to get flights operating on time. The root causes for departure delays were carefully analysed by top management and a number of aggressive targets, that were comparable to US and European standards, were laid out for the SAA staff to meet. To further motivate improvement in departure times, a number of incentive programmes were put into place to encourage staff to meet, or better, these targets.

Research showed that, in 1998, the major US airlines averaged 76% on time performance, while their European counterparts averaged approximately 77%. SAA decided to set even higher targets than these: 91 % on time for domestic flights, 87% on time for African regional flights, and 80% on time for international flights.

While SAA was trying to improve on time performance, they cancelled almost all their marketing activities. With the exception of a few tactical radio spots from time to time, virtually all of the television, radio, print, billboard and other marketing that had been planned for September 1998 through February 1999 were cancelled. SAA wanted their customers' experience to be significantly improved first. The money that was not spent on marketing during that period was instead spent on making substantial and immediate improvements to the product.

SAA next, in mid 1998, launched a two-part marketing effort, initially listening to the public. It was self critical in the campaign, poking fun at its own weaknesses like long queues, bland food, and late flights. Under the banner "*Go ahead, tell us what you think*" [33], the message was honest about wanting to learn from the customer, and aspirational about wanting to build a better airline. Research then showed that consumer views were starting to change and the dated image of SAA as the unchanging parastatal began to be replaced by a customer view that something was happening at SAA and that they really were working to build a better airline.

Andrews recognised that employees needed one major victory as a boost of confidence. That victory came in the form of SAA reaching and passing its own on time targets early in 1999, achieving on time figures better than the best US and European carriers. The results showed that more than 94% of SAA's domestic flights, over 88% of African regional flights, and 84% of SAA's international flights departed on time. SAA rewarded its staff with a bonus for 100% attendance records. It also gave three cars away in a draw for these employees. The success in meeting and exceeding the on time targets helped to create a more positive attitude amongst employees and improved confidence in the organisation to embrace the challenges that lay ahead.

The second part of the marketing campaign was to tell the public about the real improvements in customer service, starting with the extraordinary news about on time performance. The customers' actual experience of SAA flights almost always leaving on time meshed with the perceived experience through the on time marketing campaign, thus serving to reinforce each other. Customer ratings shot up quickly and SAA is now setting the world standard for on time departure performance.

Later, other action steps to improve customer service included completely retraining frontline staff such as Pursers and On-board Leaders and selecting a new cadre of first and business class Senior Flight Attendants.

Revenue Management

While customer service levels and on time performance were being improved, management restructured the national sales team by closing down smaller reservations offices and reviewed the sales department's strategy. Research into the travel marketplace revealed that 20% of the travel agents in the industry were responsible for 80% of the financial return for the airline. SAA therefore saw the immediate need to streamline its efforts and embarked on a policy of Key Account Travel Management.

Passenger counts showed an average year-on-year decline of 11.5% a week during late 1997 and the first half of 1998, and a record 24% decline in the week Andrews joined the airline (See Figure 2 for year on year growth/decline in domestic passenger count). During the latter part of 1998 and early 1999, SAA intensified its price war with domestic competitors by cutting domestic fares to regain lost market share. The price war was to some degree successful in that Sun Air ceased operations in August 1999, and the market was left with three main players: SAA, BA/Comair and Nationwide.

Revenue management for Andrews involved 'putting the right person, paying the right price, in the right seat, at the right time' and SAA acquired some of the most sophisticated software tools to assist in achieving this. Andrews also brought in some of the most highly regarded revenue management experts in the world who re-trained a team of nearly 50 employees which enabled them to substantially improve load factors and passenger mixes.

By October 1998, domestic counts were showing average weekly rises of 16.5% and international counts were climbing. Passenger revenue increased by R686 million or 24% over the first six months of the year. This increase was attributable to both passenger numbers and yield improvements. Domestic passenger numbers increased by 13% between September 1998 and March 1999, compared to the previous six months. Yield improvement for 1998/99 increased by 8% compared to the previous year and the international operations showed an increase in passenger numbers of 11% as well as a 16% improvement in yields over the previous six months.

The improvements in revenue management and passenger counts led to a sharp improvement in the profitability of the airline. In the quarter to December 1998, SAA made a profit of R8 million compared with a R24 million loss in the corresponding period of 1997. In the first quarter of 1999, SAA achieved a profit in excess of R50 million compared to a loss of R82 million in the first quarter of 1998.

While the initial focus of improving revenues was on the passenger side of the business, the focus later shifted to cargo. SAA Cargo operated as a separate business unit within SAA and was important contributor to the overall profitability of the airline. There were two distinct business sectors to the cargo operation: selling belly space on scheduled passenger flights and operating dedicated freighter aircraft on a charter and scheduled basis. Belly cargo operations had minimal incremental costs and therefore could significantly contribute to the overall airline cash flow. Freighter operations, on the other hand, were much more competitive requiring heavy load factors to ensure high yields and greater management resources.

In order to maximise profitability SAA Cargo reviewed its operational strategies. They decided to downsize freighter operations to maximise profitability and to optimise belly revenues through pricing, yield management, new products and strengthened marketing and sales capabilities. They also increased outbound market share by focussing on their top 20 to 30 local customers and improving the service levels to these loyal customers.

In addition to the central Call Centre in Johannesburg, a new Call Centre was established in Durban in March 1999 to manage more than 100 000 calls per month from the other provinces in South Africa. Employee incentive schemes were introduced to improve productivity and achieve higher profitability. A target of 15% monthly sales growth was set for reservations staff for the year 2000. By rationalising its call reservation system and targeting direct business to the airline, SAA both reduced its distribution costs (which account for as much as 15% of an airline's expenses), and increased its revenues. SAA sought to further improve revenues through direct selling on the Internet and by exploring the possibilities of e-commerce solutions.

Cost Reduction

From his first day at SAA in June 1998, Andrews aggressively attacked costs and within weeks had saved the airline about R11 million by switching to a more efficient method of purchasing. In early 1999, the cost reduction programme gained momentum and all expenditure was assessed in the light of three criteria. First, was it needed for safety? Second, did it directly benefit employees and customers? Third, were passengers prepared to pay a premium for it? If the expenditure did not meet any one of these three criteria, it was eliminated (See Table 2 for SAA performance measures between 1995 and 1999).

From the beginning, Andrews engaged all employees in appreciating the extent of SAA's financial distress. This included discussion with the various employee unions, where he made it clear that unless productivity levels improved and costs were reduced, the airline could face failure. After extensive informal meetings with employees and consultation with union leaders about 1400 jobs were shed by the end of 1998. About 1200 of these were through offering voluntary departure packages to employees and another 200 through retrenchment packages.

Next, international routes that were loss making were identified and terminated. These routes had costs that were similar but revenues that were lower than competitors, and included Osaka, Dubai, Copenhagen, Amsterdam and Dakar. Around R60 million was saved through terminating these unprofitable international routes

Purchase savings of R22 million, in the procurement of goods and services, were achieved in the period August 1998 to March 1999, and by March 2000, a further R140 million was saved. Restructuring of international commissions resulted in savings of R34 million by the end of 1999. A further R80 million was saved by optimising cargo routes and leveraging the joint venture cargo agreement with Lufthansa to increase inbound market share and strengthen product/destination offerings.

SAA was able to save a guaranteed R90 million by outsourcing management of its IT systems. In February 2000, SAA concluded an agreement with Atraxis, the SAirGroup company specialising in information technology, for the latter to assume responsibility for SAA's IT activities. A new company was formed for this purpose called Atraxis Africa. The agreement was scheduled to run for twelve years and involved replacing SAA's IT systems with Atraxis solutions. Certain air transport specific systems such as those used for reservations, departure control and ticketing would in future be operated from Atraxis' headquarters in Zurich while other systems would remain in Johannesburg.

An amount of R120 million was saved by the end of 1999 by refocusing the Technical Services and Maintenance Division. Other cost reduction actions included reducing the number of management levels in the organisation, and improved asset utilisation.

Strengthen the Mind and Body: November 1998 to December 1999

In its review of operations at SAA during 1998/99 the Transnet Annual Report noted:

"*The new management team has proven it is capable of turning the airline around"*.[35]

The report stated that the year under review would go down as one of maximum change for SAA due to both internal and external events; most notably the continued softening of the international markets in terms of yield due to over capacity (caused by the Asian economic crisis), a new management team and strategy for SAA under the leadership of Coleman Andrews, and the preparation for the privatisation of SAA. The report concluded:

"*SAA is turning the corner with regard to solving its service and profitability issues and is well on its way to completing a successful turnaround"*.[35]

Andrews commented in May 1999:

"The biggest money to be made in this industry is in turnarounds. The past five years have seen dramatic returns on equity as airline companies recovered from near-bankruptcy. We are at the point where the turnaround is under way but the company still has to endure some pain"[13]

Once the airline had been pulled out of its nose dive and placed on a path to profitability, SAA focussed on strengthening its human, technological and product capabilities. The first area that was addressed was that of establishing a global network of alliance partners and, at the same time, SAA prepared for partial privatisation.

Alliances

SAA worked on significantly restructuring routes to increase frequencies to key destinations in South Africa, sub Saharan Africa and the rest of the world. In the past, they had a limited network globally and flight frequency was low (2 or 3 flights weekly). Alliance partnerships allowed SAA to increase its levels of frequency by aligning itself with other airlines and their routes, thus improving service to customers through quicker transfers and travel times and 'seamless' connections. These strategic alliances not only provided added service value to passengers but also allowed for the global expansion of the airline. Rather than a disjointed approach into other continents, SAA's strategy was to move towards using other airlines' hubs on other continents with 'starbursts' of destinations radiating from major centres.

SAA's top management recognised that customers now demanded high levels of customer service, not just on board but also with regard to check in, frequency and flight availability to major destinations. The benefits of alliances for customers included through-checking of baggage to final destination, the issue of all boarding passes to the customer at first check-in, and the accumulation of frequent flyer miles for flying on any of the partner airlines.

After having reviewed the alliances that were established during the Myburgh era, in late 1998, after extensive negotiations completed in Frankfurt, Zurich, and Singapore, SAA concluded separate alliances with three of the world's premier airlines: Lufthansa, Swissair, and Singapore Airlines. These alliances formed crucial foundations in continental Europe and Asia for building and managing traffic to destinations on these Continents.

The new alliances allowed for expanded 'starburst code-share'. This meant that SAA distributed the partners' traffic from Johannesburg throughout Southern Africa, and in the case of Singapore Airlines to South America as well. In turn, between the partners, SAA's traffic was distributed to scores of destinations in Germany, Scandinavia, Switzerland, France, Austria, Italy, Spain, and other points in Europe and in Asia. The code-share agreements allowed SAA to again service those destinations which had previously been discontinued as unprofitable routes such as Osaka, Amsterdam and Copenhagen.

Another major element of the new alliance agreement made provision for innovative reciprocal wet-leasing of each other's aircraft to boost utilisation and upgrade services on routes with high load factors. SAA also benefited from these alliance agreements in terms of training programmes for high potential management and cabin crew personnel. Other elements of the agreements included joint sales and marketing initiatives and the integration of frequent flyer programmes.

To further expand the global reach of the airline also meant switching partners where necessary. SAA's existing alliance agreement with American Airlines, with Miami as a hub serving 27 cities within three hours of arrival, did not adequately meet the needs of SAA and its customers. On the other hand, Delta Air Lines with Atlanta as a hub, was able to serve 107 cities within three hours of arrival. Thus in October 1999, SAA and Delta Air Lines signed an agreement that provided for the first direct non-stop service between Atlanta and Johannesburg. The agreement also made provision for a code-share flight between New York (JFK) and Johannesburg. In addition, SAA would participate in Delta's frequent flyer 'SkyMiles Program' and from the perspective of Delta, the agreement served to fill a critical marketplace gap by creating new service options for business and leisure travellers from the south-eastern U.S. to South Africa.

The deal with Delta put in place another major building block for SAA's global alliance strategy. The deal was not without controversy, however, as the new agreement resulted in the Miami - Cape Town - Johannesburg route being replaced with an Atlanta - Johannesburg - Cape Town route. This infuriated the Cape Town tourism authorities who felt that SAA was impeding their tourism drive. SAA defended its decision and by the end of 2000 this was vindicated when the US-SA route showed a 24% rise in passengers because of the increased number of convenient connections.

In November 2000, SAA concluded a code-share agreement with Qantas, the Australian national airline. SAA was losing R70 million a year on its four weekly flights to Perth and Sydney mainly because the service offered uncompetitive connections to New Zealand and the revenues from Perth to Sydney were unprofitable. The problem with the service was that when SAA stopped at Perth about 35% of their passengers disembarked and the remaining 65% were not enough to make the 4000km flight to Sydney profitable. Rather than terminate the service, SAA hoped through the new agreement to turn its losses into a R20 million profit.

Passengers would benefit from increased frequencies and better connections to New Zealand as well as less time spent in the air. The agreement with Qantas was due to come into effect in January 2001, pending regulatory approval, and would see SAA fly the Johannesburg - Perth route and Qantas operate a non-stop Johannesburg - Sydney service.

In Africa, SAA had alliance agreements in place with Ghana Airways in West Africa and Alliance Air in East Africa. With Accra and Entebbe as the respective hubs, SAA was able to service most of sub-Saharan Africa as well as offer alternative routes to and from London. In the Southern African market, SAA's relationship with its sister companies, SA Airlink and SA Express, and its alliance with Air Namibia, allowed it to distribute international inbound traffic to all major Southern African tourist destinations.

The agreements with Lufthansa, Swissair, Singapore Airlines, Delta Air Lines and Qantas opened many new markets between South Africa and the rest of the world and supported the South African Government's drive to boost the economy through focussing on tourism. From serving 70 markets in mid-1998, SAA now served over 503 cities. These alliances, together with SAA's agreement with Varig, the Brazilian national carrier, to distribute SAA traffic from Sao Paulo to other destinations in South America, completed SAA's global alliance strategy by providing services to all continents.

Financial Restructuring and Privatisation

The partial privatisation of SAA has been in the pipeline since December 1995. The process had, however, been repeatedly delayed, mainly because no way had been found to deal with SAA's share of Transnet's total debt burden. The dimension of the debt was one of the legacies of the former Government's mismanagement of the pension funds of state owned entities. On its corporatisation in 1990, the deficit of the single pension fund of the newly corporatised Transnet turned out to be around R17 billion. Bonds were then issued by Transnet to the fund to reduce the deficit to manageable proportions.

SAA's share of the debt amounted to R4.057 billion and this left the organisation with a highly geared capital structure. A debt burden of R4.057 billion and a total asset value of R4 billion resulted in a net asset value of a mere R57 million. With a debt-equity of 90%, such a risky capital structure made SAA unattractive to potential investors. In late 1998, the

Government developed a solution to restructure Transnet's debt, and removed the major obstacle in the way of the partial privatisation of SAA.

In April 1999, SAA was corporatised when it began operating as South African Airways (Pty) Ltd, in anticipation of the partial privatisation of the organisation. In June 1999, the newly elected President of South Africa, Thabo Mbeki, announced in his inaugural speech to parliament that the parent company of Swissair, the SAirGroup, had acquired a 20% stake in SAA at a price of R1.4 billion (US$230 million). The agreement included an option to purchase a further 10% stake before November 2000, for which the SAirGroup paid R48 million. The SAirGroup pledged a broad strategic co-operation to build SAA into a top global carrier. Government believed that the link with Swissair would help SAA cement major relationships in Asia and North America while sharply improving its competitive position in Europe.

SAA believed that the SAirGroup had made a compelling case for how they could add significant value to SAA as it implemented its 'Strategy for Winning'. Swissair was widely regarded as one of the most outstanding international airlines in the world, renowned for its first rate customer service, technical excellence and strong financial performance. The deal augmented the alliance agreement signed earlier between SAA and Swissair. In aircraft acquisition and financing, SAA expected major savings to flow from the partnership. On the technical side of the business, the SAirGroup committed up to 15 wide-bodied aircraft a year to be overhauled by SAA and this alone would sustain approximately 300 jobs in the technical field and catapult SAA into the top tier of global maintenance providers.

SAirGroup CEO Phillipe Bruggiser stated:

"We have carefully watched SAA's impressive turnaround in the past year and we are convinced that SAA is well on its way to becoming one of the most successful airlines on the global aviation scene. Under the skilful guidance of MD Saki Macozoma and SAA CEO Coleman Andrews, SAA is making all the right moves in executing its Strategy for Winning. We believe that we can help take SAA further faster."[36]

In February 2000, the South African Government announced that it would take over R3.057 billion of the airline's total debt of R4.057 billion in accordance with a bill tabled in parliament. The debt would be split between the state and Transnet, SAA's parent company, with the state taking R1.333 billion and Transnet taking R1.742 billion. R610.5 million of the

R1.4 billion that Swissair paid for the 20% stake in SAA would accrue to the state as part of the debt distribution arrangement.

In late November 2000, after negotiations between the South African Government and the SAirGroup, it was agreed to extend the latter's option to purchase a further 10% stake in SAA. At the time that the 20% stake had been sold to the SAirGroup for R1.4 billion in June 1999, it implied that SAA was valued at R7 billion. The successful turnaround of SAA had caused an appreciation in its value to R9 billion and the Government now wanted more for the 10% stake which it had originally pegged at R700 million.

Develop the Heart and Soul: The year 2000

In an interview in November 1999, Andrews said:

"*I have done mostly turnarounds for most of the last twenty years and that involves going into a deeply distressed situation to make something out of it. The attraction here is that it is not just another airline turnaround. This job combines a very complicated turnaround with the overlay of what's taking place in South Africa. We have to build a great company at the same time that we are preparing a large number of leaders to carry that company forward".*[26]

At the beginning of the year 2000, Andrews believed that SAA had made about 35% of the progress needed to improve customer service and had unlocked about 30% of SAA's potential. Despite 60% higher fuel prices, higher labour costs and tougher competition from foreign airlines flying to South Africa, SAA had become more profitable. Forward hedging on fuel had saved significant costs and ticket prices had risen by around 12% since June 1999 without losing market share. New software systems had improved yield management, putting enough passengers at the right price on the correct flights.

The next areas of focus was upgrading the fleet and restructuring the maintenance capability. At the same time, to ensure sustainable growth, Andrews now wanted to focus on people, leadership and equity in order to improve the depth of management expertise and the technical competency levels in the organisation. He also wanted the re-branding of SAA as a truly South African airline to be boldly conveyed in the diversity of its staff and the new first and business class products that were being developed.

Fleet Upgrade and Standardisation

SAA had long enjoyed a reputation of a modern fleet and a dedication to front-line aviation technology. In July and November 1998, two Boeing 747-400's ordered during the Myburgh era were delivered to SAA. The acquisitions were financed with an operating and finance lease respectively. In late 1998, the order placed by Andrews' predecessor for four Boeing 777 aircraft was cancelled and instead SAA chose to acquire two new Boeing B747-400s, which were delivered in December 1998. The deal was financed with short-term US Dollar bridging finance which Transnet raised despite the negative impact that the Asian economic crisis had on emerging markets. Andrews' team managed during the negotiations with Boeing to have the $60 million deposit for the cancelled 777's offset against the new order.

SAA now had a fleet of 50 aircraft (See Table 3 for SAA's fleet in 1999). The different aircraft types each demanded their own maintenance infrastructures and pilot pools, and fleet uniformity remained a priority, as it was more cost-effective, fuel-efficient and allowed for modernisation. The plan was to modernise and standardise the domestic and regional fleet first.

The fleet composition needed to be able to service all of SAA's destinations in the most effective way, and to suit both passenger service requirements as well as cargo requirements. The fleet composition also needed to successfully address the question of rationalising the engine and aircraft types, as this had an effect on the amount of spare parts the airline had to keep in stock, the amount of training needed by technical staff and the licensing of cabin and crew.

In February 2000, SAA placed firm orders to acquire 21 Boeing 737-800 'New Generation' aircraft. Each aircraft would seat 157 passengers in a mixed business and economy configuration. SAA held an option for 20 more aircraft, which could be delivered as 737-800 models, or as larger 175-seat 737-900 models, or as smaller 125-seat 737-700 models. The new fleet would be used to service all SAA routes in South Africa as well as regional routes throughout Southern, West, and East Africa.

The decision to purchase the aircraft was the end result of an extensive process that began when SAA launched its 'Strategy for Winning' in August 1998, which included a mandate to upgrade the SAA fleet. The executive team consulted with a wide range of industry advisors and experts, including Airbus, Boeing, International Lease Finance Corporation, G E Capital Aviation Services, the Flightlease fleet management arm of partner Swissair, Bain & Company, and engine manufacturers International Aero Engines and CFM International.

Andrews commented that the decision was a crucial step in maintaining SAA's momentum under the 'Strategy for Winning'. The objective was to simplify, modernise, and standardise the Domestic and Regional fleet. The new aircraft would replace three different aircraft types (Airbus A300 at 21 years of age, Boeing 767 at 16 years of age, and Airbus A320 at 7 years of age). SAA's pilots, who were currently split into four different, costly pools for domestic/regional flying, would in future be grouped into a more efficient single pool for the new 737-800's and the existing 737-200's. Maintenance costs would be also lower with greater commonality in the fleet. In addition, with highly fuel efficient CFM 56 engines on the new Boeing's, SAA would be able to partially offset the negative effects of spiralling fuel costs, which threatened to cost SAA over R500 million more in 2000.

While awaiting delivery of new aircraft and in anticipation of a more standardised fleet, SAA established its Technical Division as a separate business unit with its own identity. Due to its geographical isolation and political isolation during the apartheid era, SAA Technical had developed a total maintenance support capacity. This competence enabled SAA technical to reach beyond the needs of SAA, and to provide a quality maintenance service to a wide range of customers including some of the world's biggest airlines. The airline was proud that it had the biggest aircraft technical facility in the Southern Hemisphere.

In June 2000, SAA began reorganising the recently corporatised Technical Division. The vast division was to be scaled down into a profit making enterprise with the goal of unlocking as much value as possible to attract foreign investment. Although the jet-engine facility was capable of full overhauls for a variety of engine types, the costs were 35% higher than if the work was outsourced, mainly because of economies of scale. European alliance partners were thus found to overhaul SAA's different engine types. SAA Technical would instead focus in the future on airframe heavy maintenance, which involved the total rebuild of fuselage, systems and powerplants, and required over 50,000 labour hours by skilled maintenance technicians.

SAA had already, since 1999, carried out heavy maintenance work on Lufthansa's long-haul fleet as part of the alliance agreement. Through its alliance partners, SAA secured sufficient work in the heavy maintenance area to keep it busy for many years. Whereas SAA aircraft accounted for 85% of the Technical Division's income, the strategy was that within five years, through the growth of the third party revenue, this would make up only 60%.

During the re-organisation effort initiated under the 'Strategy for Winning' plan, a thorough audit was carried out of SAA's stores, which held more than R1.3 billion in spares. It was found that it held more than twice the stock levels that were needed and it was decided that surplus stock would be sold off and the cash used to help pay for the new fleet. The technical division was expected to earn R1.8 billion in revenue for the year ending March 2001, and expected this to increase to between R2.8 billion and R3 billion over the next 5 years.

In July 2000, SAA took delivery of the first 3 of the new Boeing 737-800's. SAA became the first airline in the world to receive the 737-800's with advanced technology 'winglets', a 2.4 meter high aerodynamic sail at the end of each wing which increased the lifting power of the wing and extended the range of the aircraft. SAA would be able to operate the 737-800 aircraft with full passenger payloads to distant West African destinations such as Lagos, Nigeria and Accra, Ghana. Some of SAA's current fleet of 737's would be retrofitted with the advanced-technology winglets in the Spring of 2001.

Transformation of Staff

To suit the needs of the new SAA, the Human Resources Department's structure was completely redesigned to provide a specialised as well as a 'non-stop' service to the entire organisation. The human resources vision was specifically developed in alignment with, and as a support to, the 'Strategy for Winning' campaign. SAA's overall organisation structure was redesigned and implemented and became notably flatter and less complicated than in the past.

Motivation and productivity among employees increased considerably at SAA due to a number of incentives introduced by the leadership team. A firm and fair approach to discipline was implemented in the organisation and the leadership team led the way in making SAA cost effective and customer focused. Focus was placed on teamwork at all levels in the organisation. At the executive level a programme, based on the General Electric (GE) model, was put in place for performance based leadership development. Also, by June 2000, over 260 managers had completed a course on the fundamentals of airline management.

One of the issues that the SAA management team had to deal with was compliance with Government policies designed to redress the racial and gender imbalances of the past. An Employee Transformation Consultative Forum was established to work with a management commission to address the issues in this regard. Between 1999 and 2000, SAA increased the number of Previously Disadvantaged Persons (PDP's) on its leadership team from 5 to 7 (Compare Figures 9 and 10). Furthermore, PDP's were appointed as MD's of two major divisions. The number of PDP's in the Cargo executive team increased from a quarter to a half. In accordance with its Employment Equity Plan, SAA recruited 420 PDP technical apprentices over the period 1998 to 2000. The number of PDP's in team leader positions in the passenger services division also increased significantly. SAA also began procuring more of its goods and services from black empowerment companies.

A total of 29 new pilots had graduated from the Cadet Pilot Training Programme between 1994 and 1998. In 2000, the intake per year in the pilot cadet programme increased from 11 to 20 and the graduation rate increased from 45% to 100% over the previous year. Although a costly exercise, the programme provided for the airline's future needs.

New First and Business Class Product

SAA realised in 1998 that the first and business class products were outdated and needed to be revamped in order to remain competitive. It was, however, not critical to the airline's survival and so it was not until the end of 1999 that an announcement was made that SAA would spend R800 million, starting in 2000, on a new first and business class passenger product. Transnet MD Saki Macozoma announced that the spending would be over a 5-year period as SAA upgraded the first class and business class facilities on its aircraft.

The launch of the first class lounge at Johannesburg International airport in June 2000 was the beginning of the introduction of the new first class product. The lounge provided luxurious facilities including soundproof 'snooze' rooms, showers, a laundry attendant, and a business centre with all the high-tech necessities. In addition, the lounge offered a range of sophisticated dining options including even an a la carte menu.

The launch of a 'kerbside check-in' at Johannesburg International airport was designed as a curtain raiser to give first class passengers a taste of the luxury and pampering still to come. SAA also introduced a fast track through the immigration channel, allowing first class passengers to be escorted directly to the lounge. The launch of SAA's new first and business class product was part of their continuing plan to return the airline to profitability. Additional improvements that were planned included new sleeper beds on the aircraft, and further training of staff to improve the customer experience.

Future Challenges

As SAA completed its second year of operation under its 'Strategy for Winning', the company received awards for service from two highly respected international travel organisations. SAA was selected by Official Airline Guides (OAG) as one of five finalists for OAG's Airline of the Year 2000, and was also selected by Conde Nast Traveller magazine in the U.S. as one of the Top Ten International Airlines in the world. SAA was placed 7th on this list, which included SAA partners Swissair, Cathay Pacific and Thai Airways. Commenting on the awards, Andrews said:

> *"Our people have worked hard in the last year to bring this company up to top international service standards. All the credit goes to the thousands of men and women of SAA who have risen to this challenge. But we believe we still have much more work to do to reach the levels of extraordinary service to which we aspire. Building on the progress substantiated by these prestigious awards, our passengers, and those who have not yet experienced the new SAA, can look forward to major advances in the new year."*[24]

Observers pointed to the fact that the triumphant announcements of the awards and the profit swing of R700 million, were made against the backdrop of SAA's alleged involvement in competitor Sun Air's demise, and an angry 200 page report by black middle management which alleged that Andrews had stifled racial transformation, promoted nepotism and raised labour costs instead of cutting them.

Andrews, responding to media criticism, said:

> "*To say this turnaround is a flash in the pan is armchair analysis. Swissair tore SAA apart before it put up R1.4 billion for a 20% stake and R48 million for an option on a further 10%. It paid what it paid for a turnaround."*[19]

Coleman Andrews and his team had rescued SAA from near failure. At the end of 2000, Andrews saw the challenges that lay ahead as coping with deteriorating industry conditions brought about by higher fuel costs, overcoming the excess capacity on major international routes that was leading to declining yields (See Figure 4 for percentage growth/decline in turnover and profits), and completing the fleet upgrade. He regarded the biggest task of all as delivering improved service on a consistent basis.

Another task was preparing the airline for full privatisation and an IPO. However, Andrews was unsure as to when this would happen and said that it was up to the Government to decide. He ventured a timetable on when he expects the turnaround to be finished:

> "*Within two years we expect to be competing in the top tier of the world's top seven airlines*"[37].

As SAA spread its wings to become a major global player, it was clear that many challenges remained.

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Table 1: SAA Financial Performance 1991 - 2000

	1991/92	1992/93	1993/94	1994/95	1995/96	1996/97	1997/98	1998/99	1999/00
Turnover	R 2,920	R 3,009	R 3,273	R 3,999	R 5,013	R 5,680	R 6,364	R 7,664	R 8,836
Net profit/(loss) after finance cost	__	__	(R 23)	R 217	R 324	(R 323)	(R 244)	R 51	R 431
Total operating assets	__	__	__	R 4,355	R 5,175	R 5,320	R 6,011	R 7,795	__
Capital expenditure	__	__	__	R 115	R 918	R 535	R 582	R 1,725	__
Passenger Volume in 000's	5,000	4,770	4,750	4,800	5,200	5,019	5,150	5,310	__
Freight Volume in tonnes	220,000	270,000	330,000	250,000	260,000	350,000	353,000	360,000	__
Number of employees	11,499	9,226	8,766	10,367	10,574	11,598	10,235	10,331	__

Note 1: Amounts in Millions of Rands

Note 2: Financial Year is from 1 April to 31 March

Source: Transnet Annual Reports (for 1991 to 1999) and SAA website (for 2000)

Table 2: SAA Performance Measures 1995 - 1999

	UNITS	1995/96	1996/97	1997/98	1998/99
ECONOMY					
Total operating cost per available seat km	Cents	26.3	29.7	29.2	33.9
Personnel cost per available seat km	Cents	6.2	6.2	6.1	7
Fuel cost per available seat kilometre	Cents	3.9	5.4	5	5
Exchange rate effect	%	2.9	22	5.36	23.21
Fuel price effect	%	10.5	17.6	-10.72	-28.32
Effective change (per litre)	%	13.7	43.5	-5.94	-11.68
EFFICIENCY					
Total operating cost per revenue passenger km	Cents	37.7	46.3	45.8	47.9
Personnel cost per revenue passenger km	Cents	8.9	9.7	9.5	9.9
Turnover per employee	R'000	483.9	542.9	587.6	597
Available seat kilometre per employee	mil. Km	1.9	2.1	2.2	2.3
EFFECTIVENESS					
Revenue passengers	R'000,000	5	5	5	5
Passenger income per revenue passenger km	Cents	31.1	34	35.3	56.5
Market share: domestic	%	73	63	58	54
Market share: international	%	36	35	34	33
Market share: regional	%	35	33	35	36

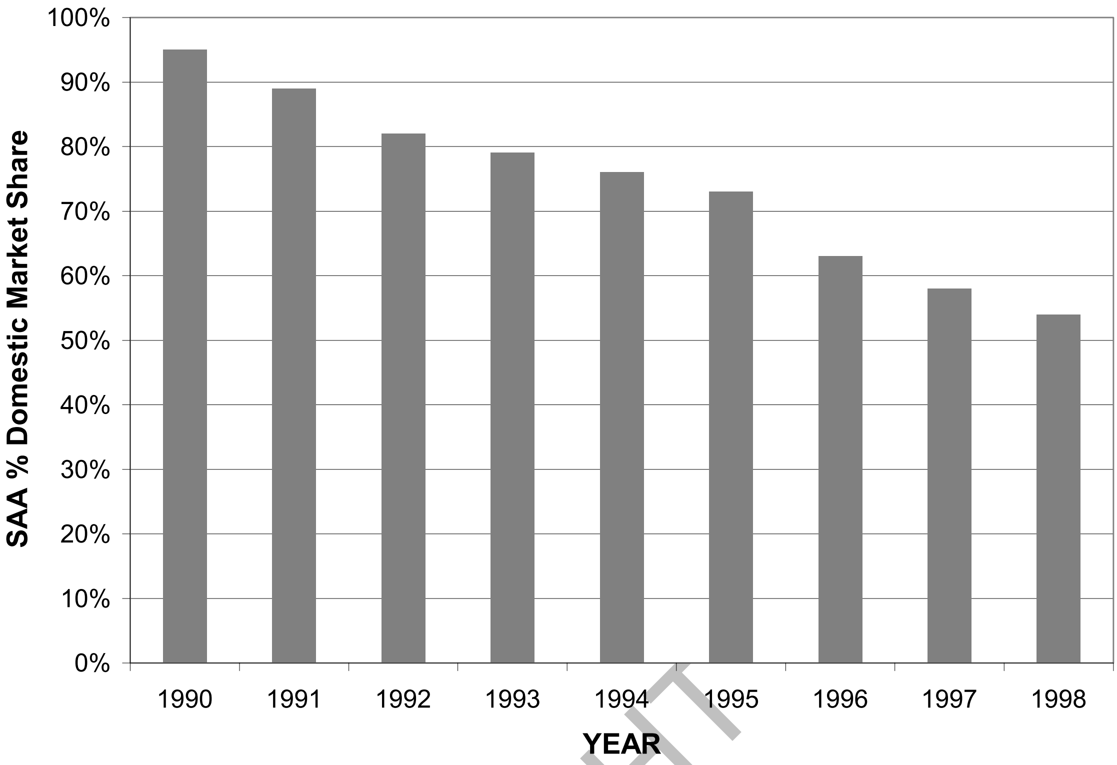
Source: Transnet Annual Reports

Table 3: SAA Fleet 1999

Passenger	**Number**
Boeing 747-400	8
Boeing 747-300	4
Boeing 747-200	5
Boeing 767	3
Boeing 737-200	11
Airbus 300	7
Airbus 320	7
Cargo	
Boeing 747-200	2
Boeing 737	2
Airbus 300	1
Total	**50**

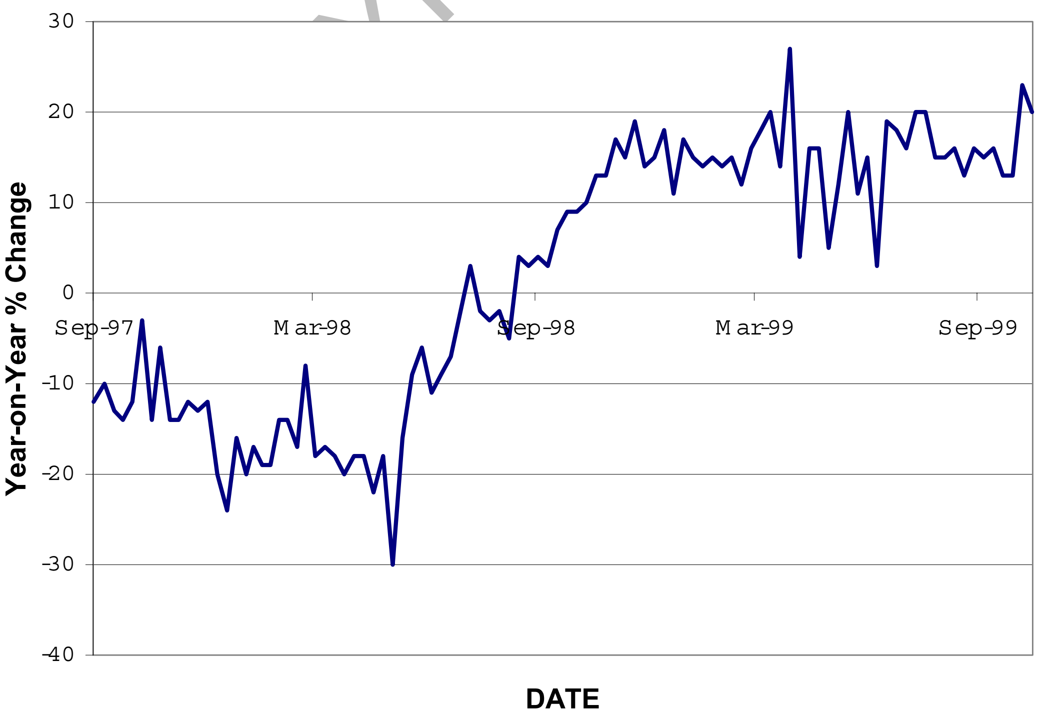
Source: 'SAA at a glance', Corporate Newsletter, August 1999

Figure 1: SAA Domestic Market Share 1990 - 1998



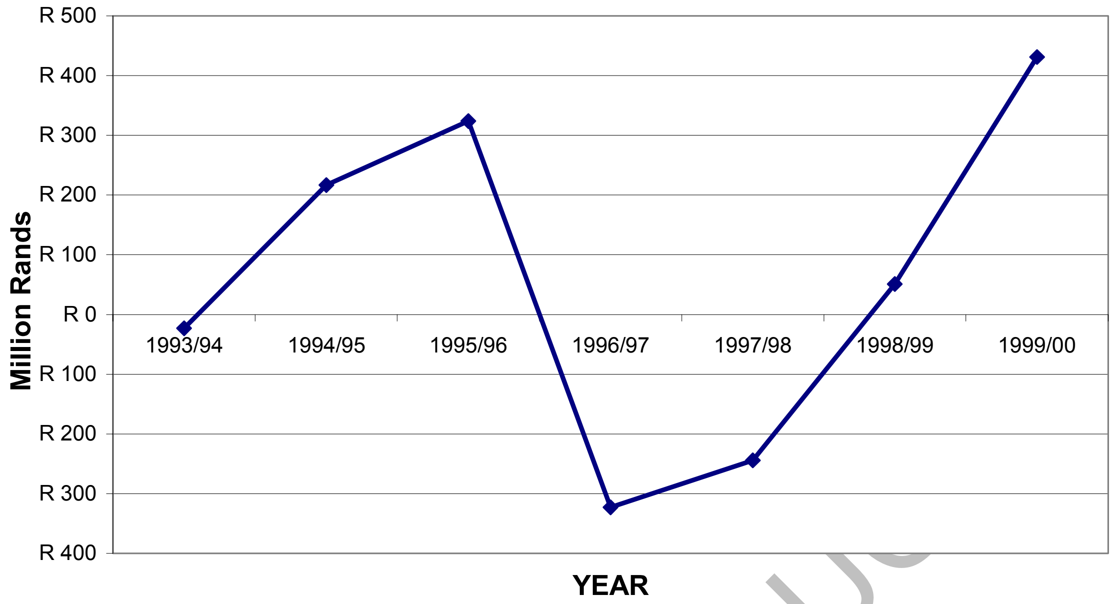
Source: Constructed from various sources

Figure 2: Growth/Decline in SAA Domestic Passenger Count 1997 - 1999



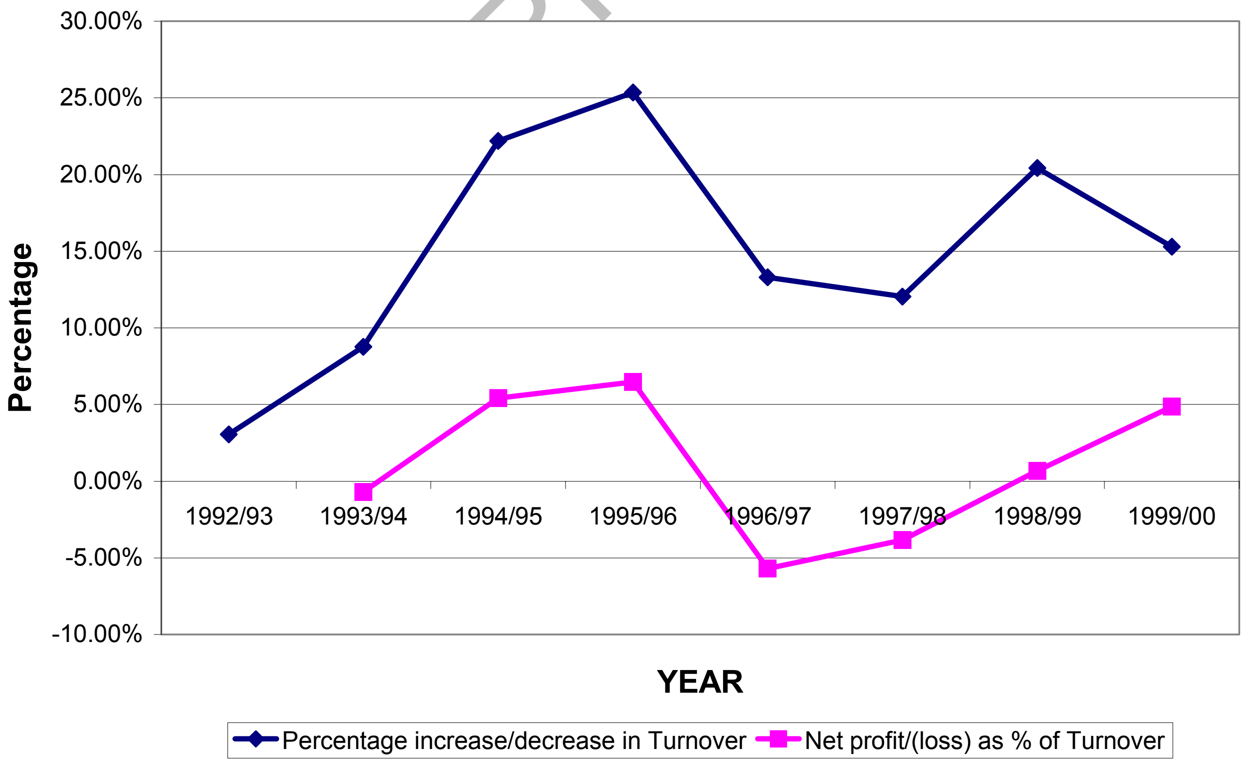
Source: Financial Mail. (2000). Coleman's Red Hot Touch. February 18.

Figure 3 : SAA Net Profit/Loss After Finance Cost 1994 - 2000



Source: Transnet Annual Reports

Figure 4: Percentage Growth/Decline in Turnover and Profits 1992 - 2000

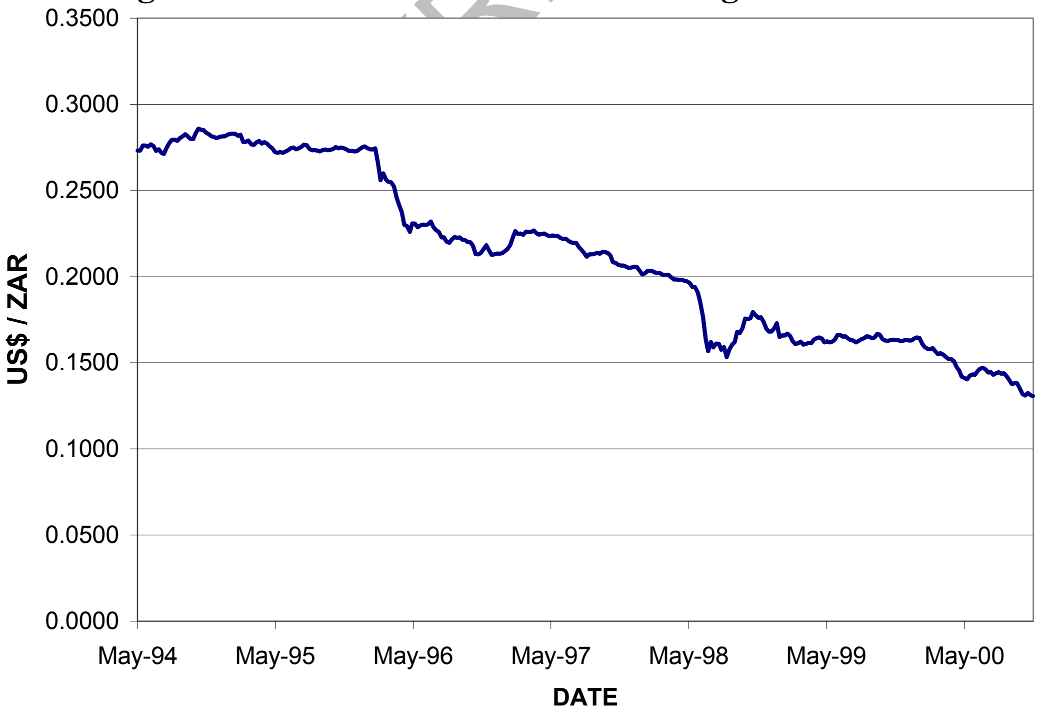


Source: Transnet Annual Reports

Figure 5: Brent Oil Spot Price in US$ per Barrel 1994 - 2000

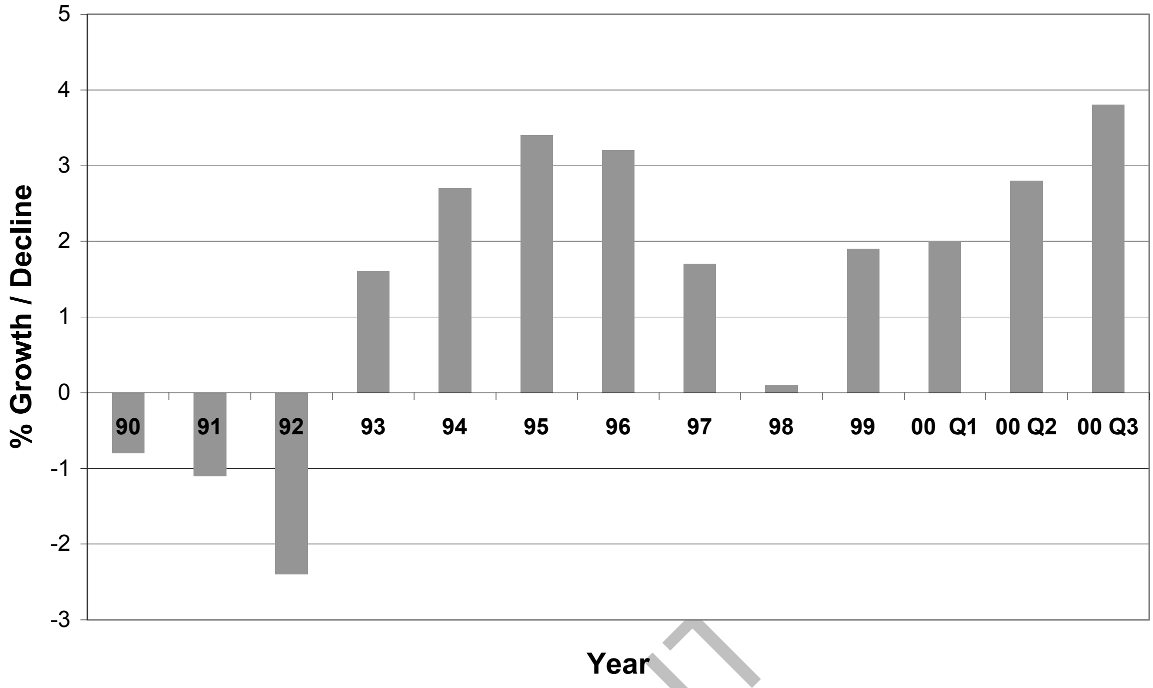
Source: BFA RAID Station database, University of Pretoria, November 2000.

Figure 6: US Dollar / SA Rand Exchange Rate 1994 -2000



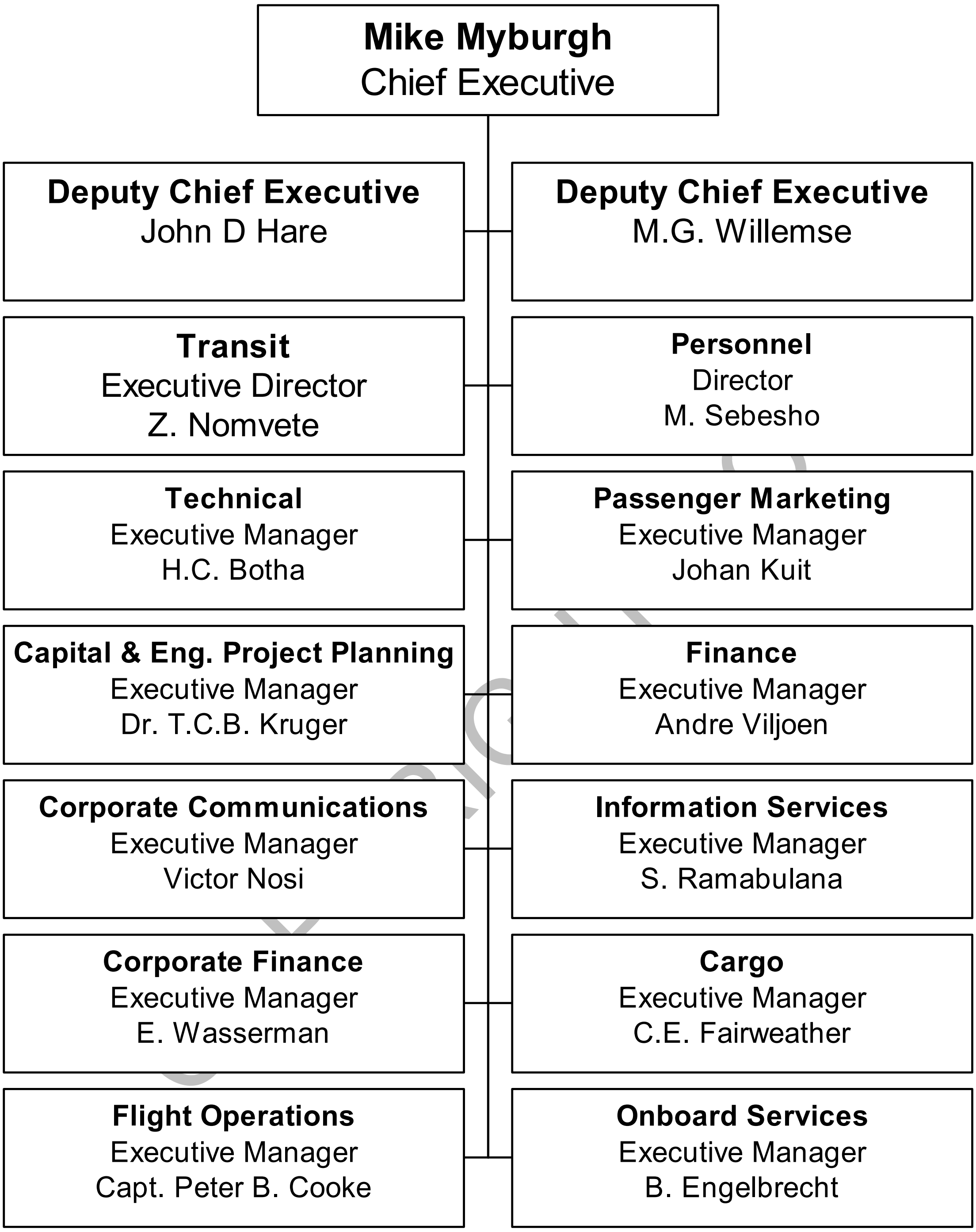
Source: BFA RAID Station database, University of Pretoria, November 2000.

Figure 7: South African GDP Growth 1990 - 2000



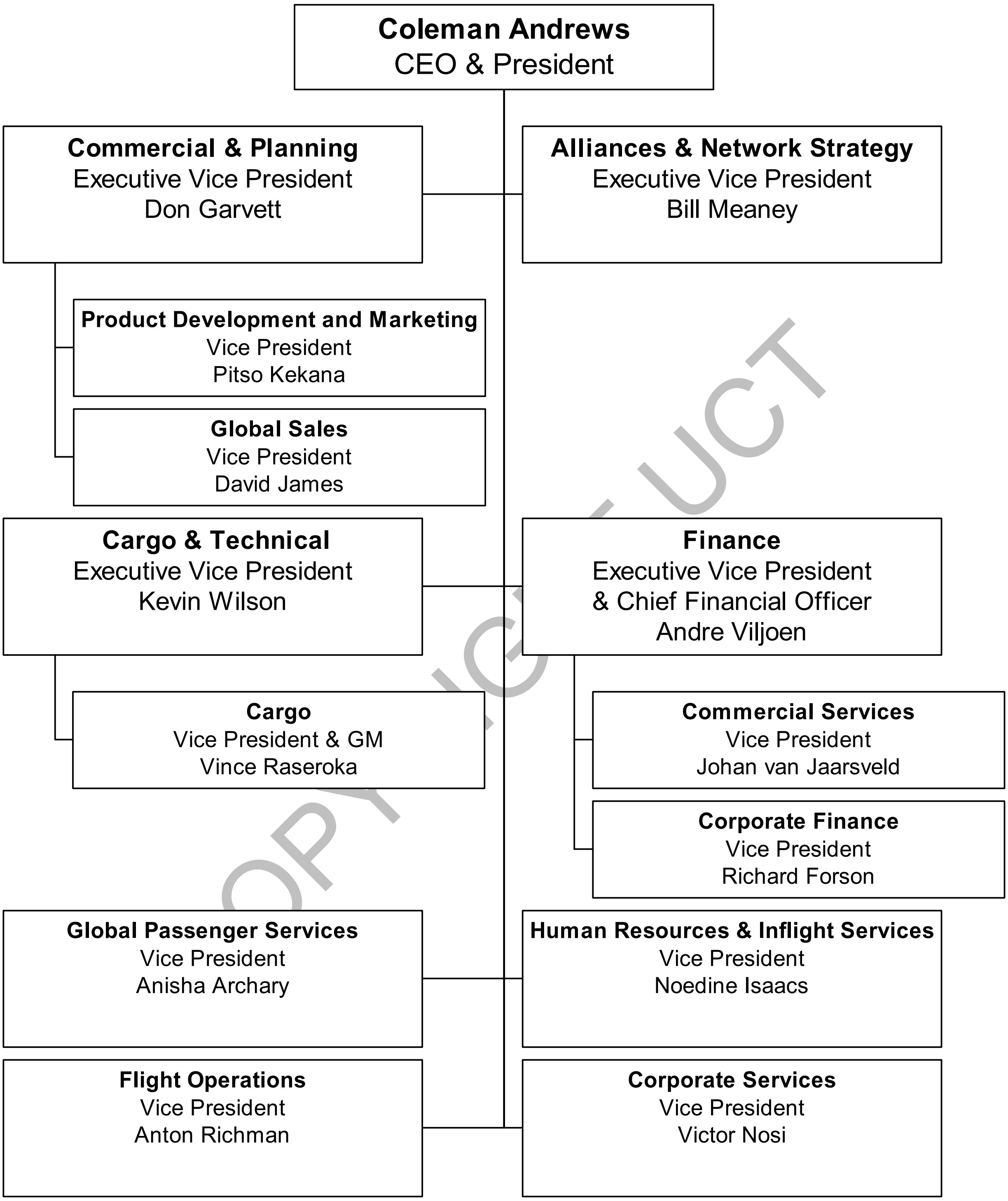
Source: Statistics South Africa (www.statssa.gov.za)

Figure 8: SAA Top Management Structure April 1998



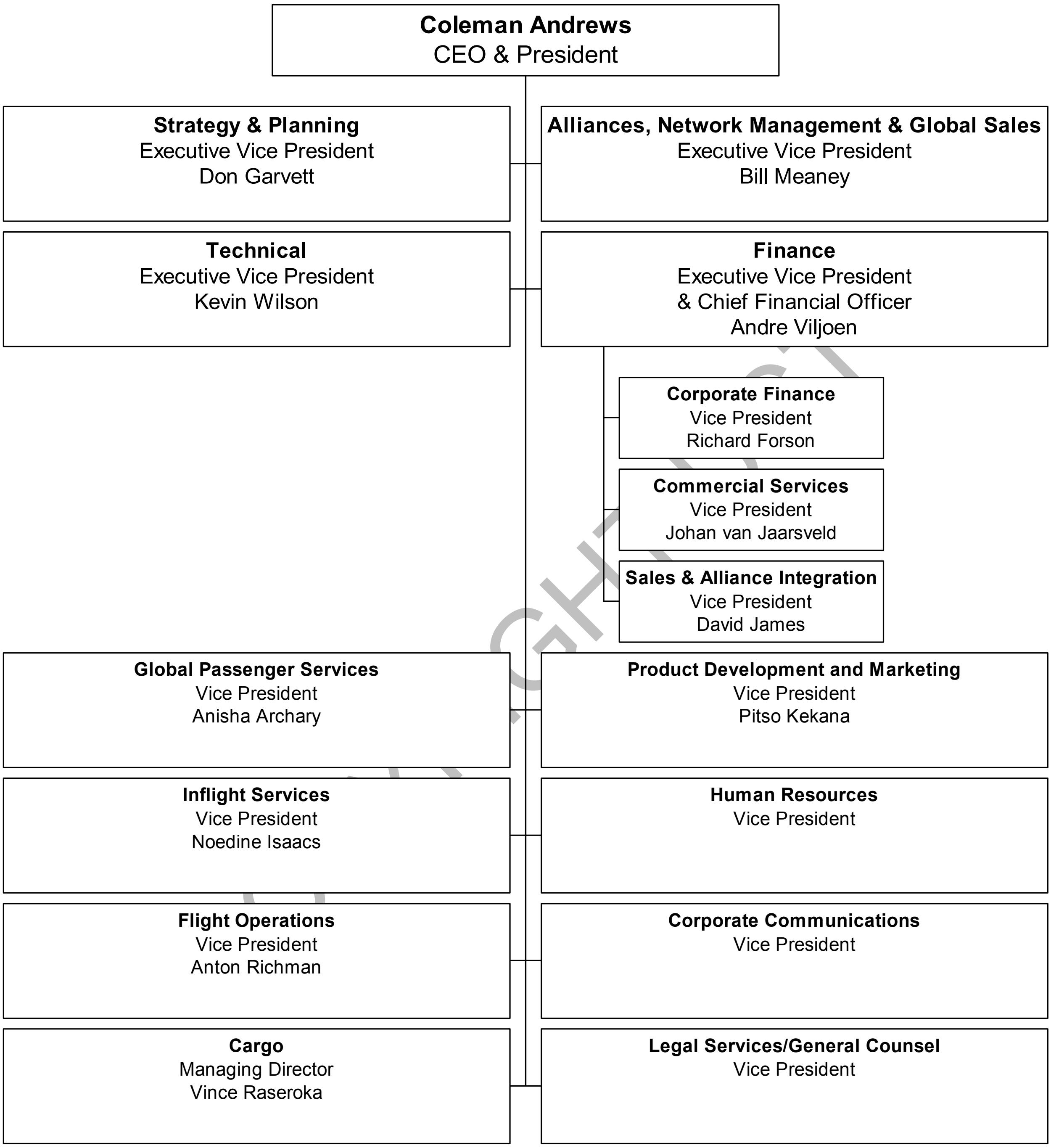
Source: World Airline Directory, 1998

Figure 9: SAA Top Management Structure August 1999



Source: 'SAA at a glance', Corporate Newsletter, August 1999

Figure 10: SAA Top Management Structure May 2000



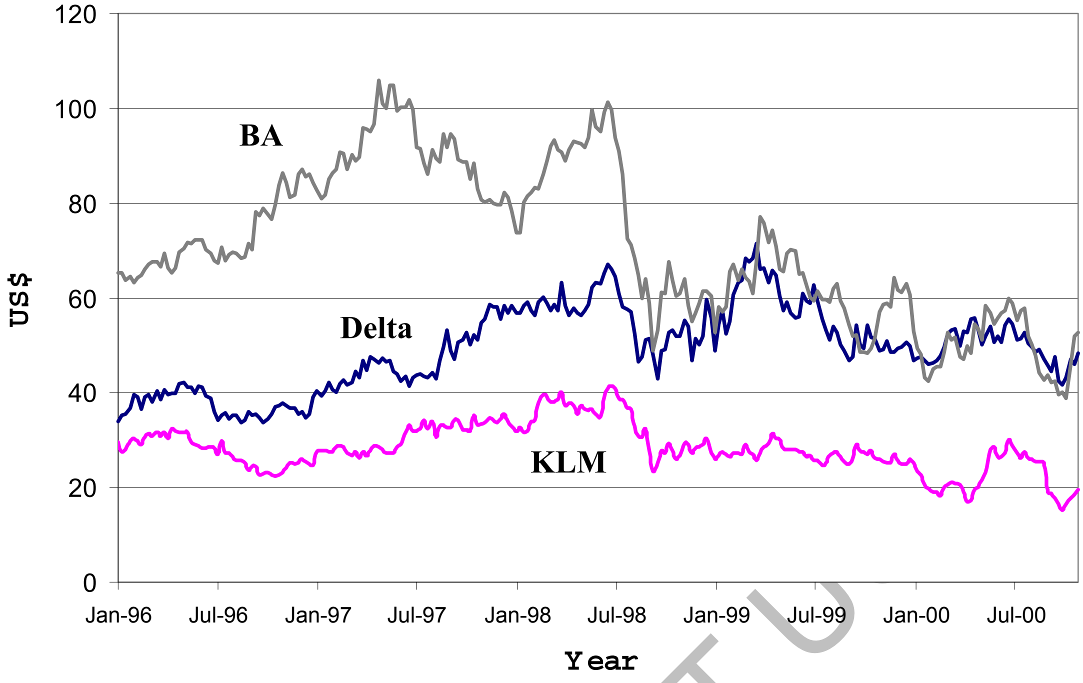
Source: 'Flight Path' - SAA Corporate Newsletter May 2000

Figure 11: Global Airline Alliances in 2000

Skyteam	Qualiflyer Group	Star Alliance	Oneworld
Air France	Swissair	Air Canada	Aer Lingus
Aeromexico	Sabena	Air New Zealand	American Airlines
Korean Air	TAP Air Portugal	ANA All Nippon Airways	British Airways
Delta Air Lines	Turkish Airlines	Ansett Australia	Cathay Pacific
	AOM	Austrian Airlines	Finnair
	Crossair	British Midland	Iberia
	Air Littoral	Lauda Air	Lanchile
	Air Europe	Lufthansa	Qantas
	LOT Polish Airlines	Mexicana Airlines	
	Volare Airlines	SAS Scandinavian Airlines	
	PGA Portugalia Airlines	Singapore Airlines	
		Thai Airways International	
		Tyrolean Airways	
		United Airlines	
		Varig	

Source: Constructed from various sources

Figure 12: Share Price Performance of Selected Global Airlines 1996 - 2000



Source: Yahoo Finance

Figure 13: Global Market Share of Selected Airlines June 2000

AIRLINE	PERCENTAGE %
Delta Air Lines	6.8
British Airways	4.9
Continental	3.6
Air France	3.1
Lufthansa	3
Singapore	2.5
KLM	2.4
Qantas	2.4
Alitalia	1.5

Note: Measured in % RPK's (Number of RPK's flown/Total RPK's flown by all global carriers)

Source: Merrill Lynch, 'Global Airlines Update', June 2000

Exhibit 1: Glossary of Terms

Apartheid

The word apartheid means 'separation' in the Afrikaans language. When the radical Afrikaner Nationalists triumphed in the 1948 elections, they created a vast legal superstructure to enforce separation. From then on, the apartheid system captured all South Africans in a complex, interlocking web of restrictions that controlled and limited all aspects of life. Verwoerd, who became Prime Minister in 1958, turned that policy into an ideology of national salvation, known as 'grand apartheid'. The pillars of apartheid included: the official identification of all citizens by race; the restriction of voting rights to whites in parliamentary elections; restrictions by race of areas for ownership and occupation of land and housing; control of African labour and mobility; a segregated and unequal education system, and, restricted personal and social interaction among racial groups. The process of dismantling apartheid began in February 1990 when the National Party Prime Minister, F. W. de Klerk, unbanned the African National Congress (ANC) and released Nelson Mandela and others. This culminated in the ANC being elected into Government in April 1994 and a new constitution being adopted in May 1996.

Transnet

The Government department, South African Transport Services, was transformed in a public company by the Legal Succession to the South African Transport Services Act, 1989. In April 1990, the South African Transport Services was corporatised to form Transnet Limited. Transnet is governed by the South African Companies Act and functions in every way as a public company with a Board of Directors, and is known as a 'parastatal'. The entire issued share capital is controlled by the Minister for Public Enterprises, on behalf of the Government.

The Group consists of the holding company, Transnet, and seven transport businesses as well as a number of related and support businesses. For the first five years the operations of the Company were organised into semi-autonomous divisions and business units each operating in niche markets within the broader transport sector. During 1996 the evolution gained pace when the composition of the board was restructured in line with the tenets of good governance expounded in the King Report on corporate governance. The articles of association of the

Company were amended to reflect a board that comprises seven executive directors and eight non-executive directors.

South African Airways was one of Transnet's seven transport businesses until 1999 when it was corporatised to form SAA (Pty) Ltd.

Code-share Agreement

These agreements take the form of contractual mergers. Their purpose is to help airlines to market their services jointly, to purchase jointly thus achieving benefits of increased purchasing power, and to increase market reach through the operation of a network of airlines.

Exhibit 2: SAA Vision, Mission and Values 1997

SAA Vision

"We will fly the spirit of South Africa to the world and be a role model to all people. We embody the magic of free South Africa to host a safe, warm African experience."

SAA Mission

"South African Airways is committed to being a dynamic, efficient and safe airline, caring for its employees, providing warm, personal service for its clients, the realisation of profits for its shareholders and contributing to the wider community."

SAA Values

"We empower through delegating responsibility and authority, expect high levels of performance, and reward in relation to contributions.

We exceed customer expectations the first time. We ask how things can be done, not why they can't.

We respect the equal rights of all people and promote their personal and professional growth through open contact and support. We create a sense of belonging and loyalty to South African Airways.

We are socially accountable and responsible to the needs of the community and the environment.

We act honestly, fairly and consistently according to clear guidelines and with transparent decision-making.

In everything we do, safety is paramount.

We strive for continuous improvement and better ways of doing things. We accept the risks that innovation bring.

While striving to do well individually, we always focus on the overall needs of the organisation."

THE TURNAROUND OF SOUTH AFRICAN AIRWAYS: 1998 - 2000

SECTION 2: TEACHING NOTE

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TEACHING NOTE

Introduction

The case study on the turnaround of SAA may well be considered a 'textbook' turnaround. Don Garvett, SAA Executive Vice President Strategy and Planning, says: *"This has been a case history of a successful turnaround"* (UMI Air Transport World, 2000). There is a high degree of alignment between the turnaround process and action steps that Coleman Andrews pursued and turnaround theory. An important objective of the teaching note is therefore to explore and analyse this degree of alignment between the theory and practice of turnaround management.

The case study 'The Turnaround of South African Airways: 1998 – 2000' provides:

- A background introduction to the global airline industry and the South African airline industry
- A history of South African Airways (SAA)
- Details of the events leading up to the appointment of Coleman Andrews, a turnaround specialist, and
- Focuses on the implementation of the turnaround during the period June 1998- 2000.

The aims of the case study are to:

- Provide a practical and contemporary example of a company in the process of a turnaround
- Examine the linkages of SAA's turnaround to the turnaround theory literature.
- Analyse the causes and symptoms of SAA's decline during the period from 1995 to 1998.
- Assess, analyse and evaluate the turnaround strategy of SAA from June 1998 to the end of 2000.
- Explore the leadership style of Coleman Andrews as a success factor in the implementation of a turnaround strategy for SAA.

The topic of turnaround strategy at SAA is worthy of teaching for the following reasons. Firstly, deregulation, global competitive pressures, volatile macro-economic conditions and privatisation have been among the drivers for transformational change within the airline industry. These external factors, combined with internal issues such as operational efficiencies, management control systems, marketing strategies, and the quality of management, have seen a number of airlines face financial distress of a nature requiring a strategic management approach rooted in turnaround theory. Secondly, SAA, a state-owned airline, experienced a period of decline beginning in the mid 1990's and resulting in a financial crisis by 1998, which necessitated the application of a turnaround strategy to rescue the company. Finally, in an era where many companies are facing crises brought on by increased global competition, the study of turnaround strategy is particularly pertinent in the broader area of strategic management. The turnaround at SAA thus provides a useful case study within the South African context of a company that is considered a global player.

The study of the turnaround at SAA is useful for a number of reasons. Firstly, there are still too few contemporary case studies that have been published on turnaround management. This area of business and management strategy is of critical importance to students and managers who are faced with a 'new economy' where traditional business management strategies and business models are coming under severe pressure. With increased global competition, more volatile markets and more demanding consumers the fortunes of companies may fluctuate wildly. Such conditions may require the turnaround management approach more frequently than may have been the case previously. Secondly, in the area of strategy more generally, there are not many cases that have been published of South African companies. SAA is not only a well-known company in the domestic environment, but also has a reputation as a global player. Thirdly, the performance of SAA will impact on South Africa's integration into the global economy and will influence key aspects of domestic economic policy such as tourism. Fourthly, the global airline industry is in a phase of consolidation as the major airlines form strategic alliances and SAA is a key player in this process. Finally, Coleman Andrews, as an MBA graduate of Stanford Business School and a previous partner at Bain & Co, the international management consulting firm, provides a truly international flavour to the case study. Thus the case study will be useful not only to South African students and managers, but will be easily received by a broader audience.

Six questions could be posed:

1. Identify the main triggers driving change in the South African airline industry?
2. Analyse the symptoms and causes of SAA's decline?
3. Identify and evaluate the key actions that Andrews took in developing and implementing a turnaround strategy?

4. How critical was Andrews' leadership style in the implementation of the turnaround?
5. What were the key success factors in the turnaround?
6. What future challenges remain for SAA and what strategic steps has Andrews taken to ensure succession and the sustainability of the turnaround in the medium to long term?

Question 1 challenges students to consider the external triggers that drove change in the South African airline industry in the early 1990's. This will help to contextualise the issues that SAA faced later on. **Question 2** will ensure an understanding of the internal and external factors leading up to the point of SAA facing the need for turnaround, a critical inflection point on the organisational lifecycle curve. This leads on to question 3 which is based on the period of turnaround and allows for an understanding of the specific turnaround strategy that was adopted. **Question 3** deals with the core issues of the case study, by assessing the sequence of specific action steps that were taken by Andrews' leadership team in the different areas of the business to successfully turn the airline around. **Question 4** explores the role of leadership style by considering the impact of Coleman Andrews' specific leadership style on the implementation of the turnaround. To emphasise and reinforce the understanding of the turnaround strategy, **Question 5** ensures an in-depth analysis of the key factors contributing to the successful turnaround. Finally, looking forward from the year 2000, **Question 6** challenges students to consider some of the key issues that will face SAA in consolidating the successful turnaround and sustaining their profitable position within the context of ongoing developments within the global airline industry. It also allows for discussion on how SAA can become a world class airline. In addition, it allows students to apply some independent thought to the importance of succession.

The following readings are suggested as a grounding for the case study and the questions that are posed:

Reference	**Recommended**
Dunlap, A.J., Andelman, B. (1996). *Mean Business.* Simon & Schuster.	Chapters 3 - 6
Lewis, Morkel, Hubbard, Davenport and Stockport. 1999. *Australian and New Zealand Strategic Management: Concepts, Contexts and Cases.* Prentice Hall Inc. Australia.	Chapter 18
Slatter, S. and Lovett, D. (1999). *Corporate Turnaround.* Penguin.	Chapters 1 - 2
Westley, F. and Mintzberg, H. (1989). *Visionary Leadership and Strategic Management.* Strategic Management Journal, Vol. 10, 17-32. Montreal: John Wiley & Sons Ltd.	Pages 17 - 32

Question 1

Identify the main triggers driving change in the South African airline industry?

In the earlier part of the 1990's the two key drivers for change in the South African airline industry were the deregulation legislation introduced in 1990 and the re-entry of South Africa into the global community from 1990 onwards. Later the formation of code sharing agreements in the global airline industry impacted on the structure of the South African airline industry.

Deregulation

Deregulation significantly lowered the barriers to entry into the domestic market, and new entrants introduced greater rivalry in the marketplace. The increased competition in the early 1990's led to the new entrants gaining market share at the expense of SAA.

- New entrants included, at various points in the early-to-mid 1990's, Flitestar, Phoenix Airways, Sun Air, Comair and Nationwide.
- Increased competition led to frequent price wars being waged in the domestic market.
- This benefited consumers and led to growth in the domestic market, but also had the negative impact of destroying the profitability of both new entrants and SAA.
- In the case of new entrants, Flitestar went out of business in 1994, Phoenix Airways in 1995 and Sun Air in 1999.
- In the case of SAA, it suffered severe losses in 1994 and in the period 1996 to 1998, which can be partly attributed to lost revenues and having to fight costly price wars to regain lost market share.
- By 2000, three players remained: SAA, Comair and Nationwide.

Re-entry in global community

The re-entry of South Africa into the global community from 1990 onwards impacted on the local airline industry in a number of ways:

- The opening up of new international markets for the national carrier SAA.
- Increased competition on international routes as foreign airlines initiated routes to South Africa.
- Increased demand from South African business and leisure customers wishing to fly overseas.

- Increased demand from foreign customers wishing to visit South Africa as a tourist destination.

Alliances

In line with the consolidation taking place in the global airline industry through the formation of code-sharing agreements, the combination of deregulation and re-entry into the global community led to the formation of alliances between domestic players and global players. Thus alliances were formed between Sun Air and Virgin, Comair and BA, Nationwide and Sabena, and SAA and Lufthansa.

Question 2

Analyse the symptoms and causes of SAA's decline?

The early to mid 1990's were probably the most turbulent period in the more than 60 years of SAA's existence. A combination of external and internal factors triggered the decline of the organisation during the period 1995 to 1998.

Corporate decline can be identified by a number of **early warning signals** such as declining margins, declining percentage of market share, declining working capital, and rapid increase of debt. In terms of the causes of corporate decline, there are both external reasons, such as changes in the economic climate, competitive change, government constraints, social changes and technological changes, as well as internal reasons. Bibeault (1982:25), referring to a survey of CEO's, attributes external factors as the sole cause in 9% of the cases of corporate decline. Where the decline is traced to internal factors, management is the principal reason 85% of the time.

Slatter and Lovett (1999) distinguish between **symptoms and causes of decline**. Symptoms are the visible signs of decline within the business itself, in the financial information of the firm, and in sentiment in the capital markets. Causes are the underlying reasons for decline that are manifested in the symptoms. They use the analogy of a sick patient to argue that those charged with the turnaround need to identify the underlying root causes of the firm's decline in order to develop an action plan. It is interesting to note that both Coleman Andrews and Slatter and Lovett use the metaphor of a sick patient requiring attention to describe the various phases of the turnaround process. The case study frames the years 1995 to 1998, during the Myburgh era, as the period of decline of SAA. However many of the symptoms of decline were evident before this period, and some of the causes can be traced back to at least the beginning of the decade.

Symptoms of Decline

Using the framework proposed by Slatter and Lovett, the symptoms of decline can be observed both within SAA itself and in terms of its financial performance. In the third area that Slatter and Lovett identify, that of signals in the capital markets, there are fewer detectable symptoms in the case of SAA, as it was a state-owned organisation and thus not a listed company.

<u>Financial Information</u>

The poor profitability and consequent cash flow crisis that is the typical, though not only, financial manifestation of a company in decline was cushioned in the case by SAA as the Government was prepared to finance the losses of the business. This may have in fact hidden the signs of decline for a longer period and thus exacerbated the underlying crisis. The financial information reveals the following:

- SAA had shown erratic returns in the period between 1994 and 1998.
- In 1993/94 the company recorded a loss of R23 million and then in 1996/97 and 1997/98 it recorded substantial losses of R323 million and R244 million respectively.
- Although in absolute terms SAA experienced growth in turnover throughout the 1990's, there was a sharp fall in the year-on-year growth in turnover in the period 1995 to 1998, which contributed to the reported losses.
- The company had attracted a high financial risk profile due to its high debt-equity structure of 90% and this may be considered a further possible symptom of decline.
- Between 1995 and 1998, SAA's domestic market share declined from 73% to 54% and its international market share declined from 36% to 33%.
- In the case of domestic market share, this factor indicates that the price wars that SAA fought during the Myburgh era with domestic competitors were largely unsuccessful in that market share continued to be lost.
- In the case of international competition, it indicates that SAA was not strategically well-positioned to take advantage of developments in the global airline industry.

Signs of decline within the business

Within the business itself, the symptoms of decline can be seen in the following:

- Low productivity levels and low morale of staff
- The lack of strategic focus of management
- Poor relations between management and employees
- Poor public image
- Negative customer perceptions
- Failure of new product launches (unprofitable routes, first and business class upgrade unsuccessful)
- The formation of factions at a middle management level
- The failure of change initiatives
- The turnover in senior management and loss of key staff
- Tension between SAA management and Transnet directors
- Poor customer service
- The lack of visionary leadership
- Loss of credibility of senior management
- Weak alignment between strategic and operational objectives
- No sense of urgency
- Management paralysis.

Capital markets

The issue of **Transnet's and SAA's high debt position** received much public attention between 1995 and 1998 and was only resolved in 1999. It suggested that SAA was not in a strong financial position and therefore risky. It contributed to uncertainty about SAA in the capital markets and **delayed the privatisation and future funding** problems of SAA.

External Causes of Decline

Having discussed the symptoms of decline, the next step is to analyse the causes of decline. Using the approach of Slatter and Lovett, the causes may be categorised into internal and external. Although the period of decline occurred between 1995 and 1998, some of the root causes of the decline can be traced back to the late 1980's and the beginning of the 1990's.

The external causes of decline include government, competition, changes in market demand and adverse movements in commodity prices.

Government

The domestic political environment had a profound impact on the environment in which SAA operated and on the internal culture and performance of SAA. From the early 1960's until the early 1990's, as a result of the apartheid policies of the National Party Government, South Africa suffered from political, economic and social isolation by the international community. Some of the **consequences of international isolation** were that:

- SAA was denied landing rights in many countries. This placed severe limitations on the growth of SAA.
- The airline was forced to develop its own technical and maintenance capabilities as sanctions prevented many countries for trading with South Africa (which may be considered to have been a positive development).
- The United Nations oil embargo against South Africa resulted in artificially high domestic oil prices, impacting negatively on the competitiveness of the airline.
- In a broader context, the isolation of South Africa created an insular mentality and culture within SAA and prevented the organisation from operating according to best practices that had developed in the global airline industry during that period.

The fact that SAA was a state-owned enterprise meant that the Government exerted undue influence in the running of the airline. Since SAA was a division of a larger parastatal, Transnet, many of its **top managers were appointed out of the ranks of the railways** and thus the organisation did not have management depth specific to the airline industry.

The year 1990 represented a landmark in the history of the country and of the airline industry. In February 1990, Nelson Mandela and others were released from prison, and the African National Congress (ANC) and other anti-apartheid organisations were unbanned. This was the beginning of a process of transition to a democratic government, which culminated in the election of a new government in 1994, and the adoption of new constitution in 1996. The **political transition** had both a positive and a negative impact on SAA:

- On the **positive** side, South Africa began in the early 1990's to re-enter the global community of nations as sanctions and other restrictions were lifted. This provided the airline with the opportunity of entering new markets. The transition to democracy also caused an increase in demand both from foreigners wishing to visit South Africa as a tourist destination, and from domestic business and leisure customers wishing to explore the opportunities that had opened up for the country.

- On the **negative** side, the transition caused great uncertainty within the state apparatus and led to a situation of near paralysis within state-owned enterprises. In the run-up to the 1994 elections the country experienced increased labour unrest, which had a negative impact on the productivity and efficiency of the airline, and caused mistrust and tension to develop between the airline's predominantly white management and its predominantly black workforce.

During the early period of the transition, the ANC had propounded socialist-leaning policies, but as the elections approached ANC policy began shifting towards the **privatisation of state assets** in order to stimulate economic growth and provide the new Government with funds for its Reconstruction and Development Programme (RDP). The ANC's strongest ally, the Congress of South African Trade Unions (COSATU) resisted this **shift in policy**, and this resulted in no clear directive emerging on the privatisation of SAA until 1996. The uncertainty caused by the political transition can be considered to be one of the primary causes of the decline of SAA, because of the multiple effects it had on the character and performance of the organisation.

It is interesting to note that in the post-1994 period there is **little evidence of major labour unrest** contributing to the decline of SAA. This is partly explained by the fact that as a state-owned enterprise, the new Government was willing to concede more readily to the demands of labour, given its strong alliance with COSATU. This implies that the SAA workforce increased its bargaining power after 1994. While labour unrest may have decreased, **labour costs rose**, resulting in higher costs for the airline. **Labour also became more inflexible** in terms of hours of work and this had a negative impact on productivity and costs. These factors certainly did contribute to the decline. A further impact of the transition was that as calls for **affirmative action** increased, the credibility of the still largely white management decreased. While SAA took various measures to move away from its old image, the pace of change was too slow.

Competition

The year 1990 represents a landmark for another reason; the South African Government introduced legislation in that year to **deregulate** the domestic airline industry. This led to **increased competition** for SAA and a **loss of market share**. In 1990, SAA's domestic market share was 95%. By 1995, their share of the domestic market had dropped to 73% and to 54% by 1998. The increased competition contributed to the decline of the airline, as SAA fought **costly price wars** to regain market share.

During the early 1990's, airlines began to seek opportunities to perform contractual mergers in the form of **code sharing agreements** with other airlines. This led to a period of consolidation in the structure of the global airline industry. This helped the dominant players in the industry to increase market reach through the operation of a network of airlines. Although Myburgh focussed on the building of route networks, the strategic choices that were made and the **management of alliances were not always successful** as is evident from the poor performance of the agreement with American Airlines. Some of the international routes that SAA chose to establish during the Myburgh period turned out to be unprofitable and contributed to high costs and low revenues. Finally, a number of foreign airlines established routes to South Africa after 1994 and this led to increased competition for SAA, lower yields and thus depressed revenue.

Changes in Market Demand

The airline industry is highly price sensitive and tends to follow the global and domestic business cycles. After 1994 South Africa experienced a short period of economic growth, but by 1996 economic growth had slowed and the country entered a period of **economic recession**. The weak performance of the domestic economy was exacerbated by global economic conditions, and in particular the **Asian economic crisis** of 1998 which impacted negatively on emerging markets. These factors led to a weakening Rand, high interest rates and rising inflation. Domestic consumer demand was thus depressed. The Asian crisis also depressed demand in the airline industry as a whole.

Adverse movements in commodity prices

The poor macro-economic conditions in the South African environment, the weak Rand and high interest rates contributed to SAA paying **high prices for fuel** which made it uncompetitive. Between May 1995 and August 1996 the oil price rose from around $16 per barrel to around $24 per barrel. Although it came off this high to around $10 at the end of 1998, the poor macro-economic conditions prevented the subsequent decrease in the oil price from filtering through to consumers. Fuel prices thus remained a high and uncompetitive input cost for SAA.

Internal Causes of Decline:

The internal causes of decline that can be identified from the case include:

- Poor Management
- Inadequate financial control
- High costs
- Lack of marketing effort
- Organisational inertia and confusion

Poor Management

The poor management during the Myburgh era reveals itself in the case study in the period of decline and in the diagnosis phase of Andrews' leadership. All the other causes of internal decline identified above can be linked to the poor management. The poor management needs to be considered within the context of the turbulent external environment discussed earlier. The management during the period is characterised as follows:

- Lack of real vision
- Lack of leadership
- Lack of strategic focus
- Lack of depth and experience in the airline industry
- Poor stakeholder management manifested in the tensions between CEO Myburgh and Executive Director and Chairman Nomvete
- Inability to engage stakeholders in the privatisation process
- Low credibility amongst staff
- Poor financial control
- Poor strategic choices
- No sense of urgency
- Lack of accountability
- Bureaucratic

- Hierarchical
- Functional isolation
- Poor communication
- Paralysis

Inadequate financial control

Although attempts are later made to cut costs, it is clear that costs were generally high and uncontrolled. There is evidence in the case of corruption and nepotism. The **management control systems were inadequate** and failed to provide management with timely information. The **bureaucratic, hierarchical organisational structure** contributed to ineffective control. The **Information Systems were outdated and inadequate** to deliver the necessary analytical information.

High Costs

SAA's costs were high in terms of the **two key cost drivers** in the airline industry: fuel and labour. Due to macro-economic factors it had **high fuel costs**. Due to the strong bargaining power of employees after 1994, SAA had **high labour costs**. Due to low morale and low productivity, SAA had **poor operating efficiencies** (See Table 2 of the case study on performance measures). SAA's cargo and passenger **route networks were not optimal** and it had high costs on under-performing routes. SAA also had **high purchasing costs**.

Lack of marketing effort

Historically, there was a lack of market orientation in SAA. This was largely because as a state-owned organisation, SAA was not profit-driven and thus **did not value customers**. As a result, after deregulation it lost market share dramatically. **Customer service** was poor. There was no common theme in the marketing materials and the marketing efforts were uncoordinated. SAA **lacked a clear strategic marketing focus**. The launch of a new corporate identity during the Myburgh period failed to change the negative perceptions that the public had of SAA.

Organisational inertia and confusion

Throughout the organisation there was **no sense of urgency**. This manifested itself in poor on time performance. There was **no clear direction from the top management** and this caused uncertainty amongst employees.

Question 3

Identify and evaluate the key actions that Andrews took in developing and implementing a turnaround strategy?

A corporate turnaround according to Bibeault (1982:81) is a substantial and sustained positive change in the performance of a business. Companies that have had several years of declining profits or even substantial losses use a turnaround to break out of declining performance. SAA had suffered significant losses that were increasing and it was thus at a point approaching insolvency on the Corporate Life Cycle (Slatter and Lovett, 1999), a position where turnaround is most appropriate.

The objective of a turnaround is to rescue the company. It seeks to achieve sustained viability fast and encompasses crisis management, capital restructuring and dealing with stakeholders. In order for the turnaround to be sustainable it must address both strategic and operational issues. In addition, the rescue plan must seek to cut costs and grow revenues. To ensure sustained profitability, the perspective should be both short and long term.

Coleman Andrews in his turnaround of SAA, turned the company around sharply, moving it out of its critical position into one of profitability. He went through a number of key stages with specific steps in order to achieve this and also to ensure the sustainability and the growth of the company into the future.

'Stop the bleeding'

His first key step was the **reorganisation of the management team**. He replaced the majority of the top team by recruiting from within the company, and also with external appointees such as Bill Meaney, Don Garvett and Kevin Wilson (all Americans). He successfully surrounded himself with experts in order to develop and implement the turnaround of SAA. Dunlap (1996) suggests that getting the right management team is the first step in implementing a successful turnaround. The next step is cutting back costs and then improving revenue, and these are all steps that Andrews included in his phases. SAA's turnaround was specifically **revenue driven** with **cost cutting** playing an important even though secondary role. This ties in to Bibeault's (1982) three broad types of operating strategies: cost cutting, revenue generating, and, asset reduction.

The first phase was one of **diagnosis** which can be linked to Slatter and Lovett's (1999) initial phase of analysis. The new leadership team and Andrews identified the root causes and a number of areas such as customer service that required immediate attention. He recognised, as had Bethune at Continental Airlines, the importance of **engaging the employees and stakeholders** in appreciating the extent of the financial distress of the company. He also spoke to the employees and the customers and listened to their complaints.

Developing a real strategy is also necessary in a turnaround, and Andrews and his team developed a **"Strategy for Winning"** as an action plan for implementation of seven pillars that they had identified in the diagnosis phase.

Costs were cut immediately but the primary focus was to improve the **operational performance** of the airline. On time performance was attacked and employees were **incentivised** with bonuses for meeting and/or exceeding the targets that were set. It was only once the performance was improved that the advertising campaign could again be used effectively. The new campaign tied in to the notion of customer service. He first asked the customers to tell them what was wrong and then after improving the performance, used the advertising to align the perceptions with the new levels of service.

Andrews refers to this phase as the 'stop the bleeding" phase, where it is necessary to improve the revenues and cut costs in order to pull the airline out of its nose dive. A number of steps were taken to improve revenue. **Yield management** was improved through better systems and a focus on key accounts. Passenger numbers were increased through a number of **price wars,** targeted at domestic competitors to regain lost market share.

The focus upon **reduced sales offices** and **increased direct sales** led to a reduction of distribution costs. Again these targets were set and incentive programmes were used to motivate the employees to attain the goals. While the initial focus was on the passenger revenues, cargo revenue was also optimised by focussing on belly cargo operations, which had low incremental costs.

Costs were analysed and three questions were posed about each expense. Key to cost cutting were reduction in staff, the termination of non profitable international routes and purchase savings. A number of additional cost cutting actions such as the restructuring of international commissions, optimised cargo routes and the outsourcing of management of IT were also instrumental in the overall reduction.

'Strengthen the mind and body'

Another critical element of the 'Strategy for Winning' and the growth of SAA was the **developing of alliances**. Alliances were formed with international carriers such as Lufthansa, Thai Airways, Singapore Airlines, Swissair and Delta Air Lines. These alliances allowed SAA to increase their global reach and in addition added service value to the customers. The alliance partnerships also allowed SAA to benefit from the fleet and hubs of its partners and also to benefit from economies of scale. These strategic alliances and the partial privatisation positioned SAA to remain competitive and grow. The agreements also strengthened the financial position of the airline and the privatisation process, in particular, assisted to reduce the debt.

'Develop the heart and soul'

After the initial eighteen-month turnaround period that had seen the company return to profitability it was necessary to move into the growth phase. Andrews under his 'develop the heart and soul' phase took key steps towards **rationalising the fleet**. Improved commonalities in aircraft types significantly reduce the technical costs as well as the staff training costs.

Identifying and **developing staff** for leadership positions was also a necessary step for the future growth and sustainability of the company. Compliance with the Employment Equity Act, to redress historical racial and gender imbalances, also necessitated a number of Previously Disadvantaged Persons (PDP) appointments. SAA recruited 420 PDP technical apprentices over the period 1998 to 2000. The number of PDP's in team leader positions in the passenger services division increased significantly and PDP appointments on the leadership team increased to seven out of fourteen.

Another key strategic step in this phase was to **improve the first and business class** products. Improvements in onboard service and launches of new first class lounge and kerbside check in were successfully completed in 2000. Staff were also trained to offer improved service onboard and this was in line with the continued improvement in customer service.

Question 4

How critical was Andrews' leadership style in the implementation of the turnaround?

Andrews' leadership style was key in the implementation of the turnaround. Westley and Mintzberg (1989) suggest that the leadership style that is necessary for a turnaround in a public bureaucracy is a 'bricoleur'. According to them the bricoleur has an interactive, social ability to interpret situations and make the necessary insights. Andrews, in his diagnosis phase, by interacting with the employees and considering every aspect of the business was able to **make critical insights** into where the key problem areas lay. Andrews also has an **ability to listen** to and understand people, and take these insights and translate them into where the company can be in the future. Furthermore Andrews, like Bethune, did not make use of anything startling or new but managed the changes with a clear implementation plan ('Strategy for Winning' and 'The Go Forward Plan"). Andrews' leadership style also fits into the bricoleur in that his **strategy was an incremental one**, building on the seven pillars.

Bibeault (1982) argues that while there is no one given style for a turnaround leader there is a consistency in the pursuit of the objectives of turnaround leaders. While it is difficult to generalise about their characteristics, Bibeault identifies four required skills from his contact with turnaround leaders:

- an entrepreneurial instinct coupled with professional management skills
- broad business experience
- expert negotiating skills
- expert interviewing skills

Andrews, having founded Bain Capital in 1983, along with his business background in consulting and later in the turnaround of World Airways, certainly had the necessary entrepreneurial instinct and also the business experience. His negotiating skills are reflected in his ability to get the unions to agree with the proposed changes and reduction in employee numbers. It can be inferred from the strong new leadership team that he recruited that his interviewing skills were good.

Myburgh, the previous CEO of SAA, had introduced change initiatives and created structures to facilitate change but the initiatives lacked penetration and were not well co-ordinated. While there is evidence that Myburgh was liked by some of the staff, he was generally regarded as a weak and ineffectual leader. Andrews, on the other hand, successfully initiated and implemented the changes necessary for the turnaround, moving through Kotter's eight steps to transforming an organisation, viz.:

- Establish a sense of urgency
- Form a powerful guiding coalition
- Create a vision
- Communicate the vision
- Empower others to act on the vision
- Plan for and create short-term wins
- Consolidate improvements and produce still more change
- Institutionalise new approaches

On his arrival, Andrews **established a sense of urgency** by engaging all the employees and stakeholders (including the unions) to appreciate the severity of the situation. If the airline did not return to profitability then all the staff would face unemployment. His first step of finding key managers for the **new leadership team** was an important step in creating enough power around him to effect the change. He recognised the need for experts in the critical areas to enable the airline to change. According to Dunlap (1996) it is important that the management team is a general reflection of the leader, without being carbon copies. When looking for a team it is useful for a CEO to recruit people who have worked with him/her before and also who have been through change. Dunlap also points out that in every company there are some competent people who are buried by layers of corporate politics and bureaucracy and that by removing the shackles of bureaucracy these people can then flourish. Andrew chose experts such as Don Garvett who had been a consultant to 60 airlines and had the appropriate experience. He also found the competent people within SAA and developed and promoted them to leadership positions.

While the **vision** was already developed in the Myburgh era, Andrews identified that employees desperately needed a clear and compelling vision of what their future could be. Clarity was necessary in order to get employees to embrace the vision and work towards its accomplishment. The 'Strategy for Winning' was thus developed to communicate this vision and also as a **clear implementation action plan**. In terms of communication, like Bethune of Continental Airlines, Andrews believed in **talking to the staff** to improve employee morale. From his first day he felt it necessary to talk to the staff for at least 45mins a day in order to understand what was happening on the shop floor. This also assisted in the general communication and enabled him to get a feel of the situation at the ground level.

Andrews **empowered others** to act on the vision. Restructuring of the management structure to a flatter organisation removed the barriers of bureaucracy that were blocking the growth of the company. Andrews implemented a management team with fewer reporting lines to facilitate this. This enabled a more efficient decision making process and the implementation of the 'Strategy for Winning".

Bethune and Andrews both successfully used **incentive schemes** to motivate employees to improve operational efficiencies. **Short-term wins** with attainable goals were set in order to improve the morale and perception of the airline. Andrews' style of rewarding the staff for achieving operational efficiency improvements had further positive effects on their performance.

Once the operational efficiency targets had been met, Andrews used the advertising campaign to align the actual performance with the stakeholders' perceptions. Andrews in this regard was constantly quoted in the media, an enigmatic character he repeated the 'Strategy for Winning' constantly. He also portrayed a positive image to the press and public and frequently reiterated his ability to turn SAA around. In addition, regular corporate **communication** illustrated the link between the implemented changes and the success of the turnaround. The swing to profitability was linked to the revenue improvements and cost cutting programmes. This served to **consolidate** the improvements and motivated the staff to aspire to new, more challenging goals.

Finally, Andrews realised after the initial 2 year period when the airline was turned around to a profitable company, that it was then necessary to transform/ develop the staff to ensure sustainability. While he recognised the need for training and employee development, it does not seem that Andrews had a **succession plan** in place. This could be questioned since it forms an essential component for the long-term sustainability of the turnaround.

Question 5

What were the key success factors in the turnaround?

The are a number of requirements that are necessary for the successful implementation of change. Slatter and Lovett (1999) identify 5 key ingredients that are all necessary for the change to be successful:

- there is a need for pressure to change
- leadership and vision are necessary
- a competent and capable team / employees
- a set of actionable first steps
- effective rewards

The key success factors in the turnaround in SAA can be considered under each of these 5 ingredients. SAA had been a protected monopoly until the deregulation of the industry. In addition, as a parastatal the burden of the debt was not really felt by the organisation. For these two reasons it was important for Andrews to emphasise that the company was now accountable. He had also to emphasise the need to change, to impress the **sense of urgency** on the stakeholders and to clarify and highlight the extent of distress. Andrews successfully achieved this by communicating with the staff and through talks with the unions.

Andrews, a turnaround specialist appointed by Transnet, brought experience and **leadership** ability to SAA. He recognised that there was no clarity in terms of the **vision** of SAA. The company needed to be able to visualise where they could be in the future and actionable steps needed to implemented. The 'Strategy for Winning" developed from the vision and mission statements helped to define implementation stages and **clear action steps**. These actionable first steps if lacking, according to Slatter and Lovett (1999), will lead to frustration.

In order to implement the changes and to grow the company it was necessary to train and develop the employees. A capable and **competent management team** was the first structural change that Andrews made. He appointed from within the company and also sought expertise from external sources. Once this new leadership team was in place he started to focus on revenue and cost.

In order to motivate the employees, rewards in the form of **incentive schemes** were introduced for improved operational efficiencies. Improving customer service was the primary focus and clear targets were set for the staff to meet. Incentive schemes directly linked to improved operational efficiencies further motivated the employees to exceed expectations. Incentives for 100% attendance in the form of bonuses were also offered and in addition, 3 cars were drawn for all those employees who had received the bonuses.

Question 6

What future challenges remain for SAA and what strategic steps has Andrews taken to ensure succession and the sustainability of the turnaround in the medium to long term?

The leadership team under Coleman Andrews has been successful in returning the airline to profitability. However, in order to position SAA to become one of the top five global carriers and to take the airline to a successful Initial Public Offering (IPO), many challenges remain.

During the year 2000, the **rise in oil prices** and the continued uncertainty about the oil price had a negative impact on the airline, adding almost R700 million to SAA's costs. During the latter part of 2000, the rampant **strength of the US dollar** led to a devaluation of many emerging market currencies, including the Rand. While the domestic economy continued to show signs of recovery, at the end of the year 2000, the outlook remained uncertain. These **macro-economic conditions** created difficult trading conditions for the airline, and contributed to continued high costs. Andrews' team has opted to use **forward hedging** to better manage the risks associated with exchange rate fluctuations and adverse movements in the price of oil.

Although turnover grew during the year 2000, SAA was unable to sustain the high growth in turnover that it experienced during 1999. While SAA was able to defend its market share, it appears to have been unsuccessful in making major gains in terms of **regaining lost market share**. SAA will need to continue to build its new image of on time performance and reliability. It will also need to continue to **improve its yield management systems**. In this regard, the successful implementation of the **outsourcing** agreement with Atraxis remains a major challenge for the future.

On the international front, the number of foreign airlines competing on South African international routes grew from 21 to 60 by 1996/97. This presents a formidable challenge to SAA to retain customers and market share. While SAA had successfully established an international network of alliances, the **management of these alliances** to the benefit of SAA and **leveraging gains** from them remains a challenge for the future. The period of consolidation of the global airline industry is likely to continue for the foreseeable future and SAA will have to remain **vigilant of other alliances disrupting the alliance strategy** that it has put in place.

Within the organisation itself, Andrews took a number of successful steps to:

- Develop the depth of management experience
- Promote high potential employees within the organisation
- Develop a more customer-focussed orientation amongst employees
- Train and develop technical personnel for the future needs of the airline
- Create more diversity in the middle and senior management ranks of the organisation

The change process has, however, not been without pain. SAA will need to **nurture the new emerging culture** within the organisation in order to **sustain the momentum of change**. If SAA is serious in its intentions to be amongst the top five global carriers, then it will have to give far greater attention to **customer relationship management**, and set new standards of superior customer service. The process of **identifying a suitable successor** to Andrews in two years' time needs to begin immediately, and needs to win the approval of key stakeholders including the Government, Transnet and Swissair. This will be a key challenge for Andrews himself.

Moving into the new millennium, the major trigger for change in the industry has been the impact of **the Internet** on the marketing, sales and distribution functions of airlines. Distribution costs account for up to 15% of an airline's costs and thus represents a significant cost driver. The Internet and **e-commerce** have opened up the possibility to substantially reduce these costs through online marketing and sales. The South African airline industry has been relatively slow to respond to these developments. A future challenge for SAA will be the **successful roll-out of its new interactive website**. Students are encouraged to visit and evaluate the SAA websites:

http://www.saa.co.za

http://www.saa-canada.com

http://www.saa-usa.com

http://www.saairways.com.au

Lecture Structure and Timing

The discussion and timing for a two-hour lecture is given below:

Discussion	**Time (in minutes)**
Introduction	5
Triggers for change in the global and SA airline industry	15
Symptoms and Causes of SAA's Decline	20
'Strategy for Winning' Implementation Action Steps: 'Diagnosis' and 'Stop the Bleeding'	20
Break	10
'Strategy for Winning' Implementation Action Steps: 'Strengthen the Mind and Body' and 'Develop the Heart and Soul'	20
Andrews' leadership style	10
Key Success Factors in the Turnaround	10
Future Challenges	10

The **accompanying figures A to J** will assist with the presentation of the lecture.

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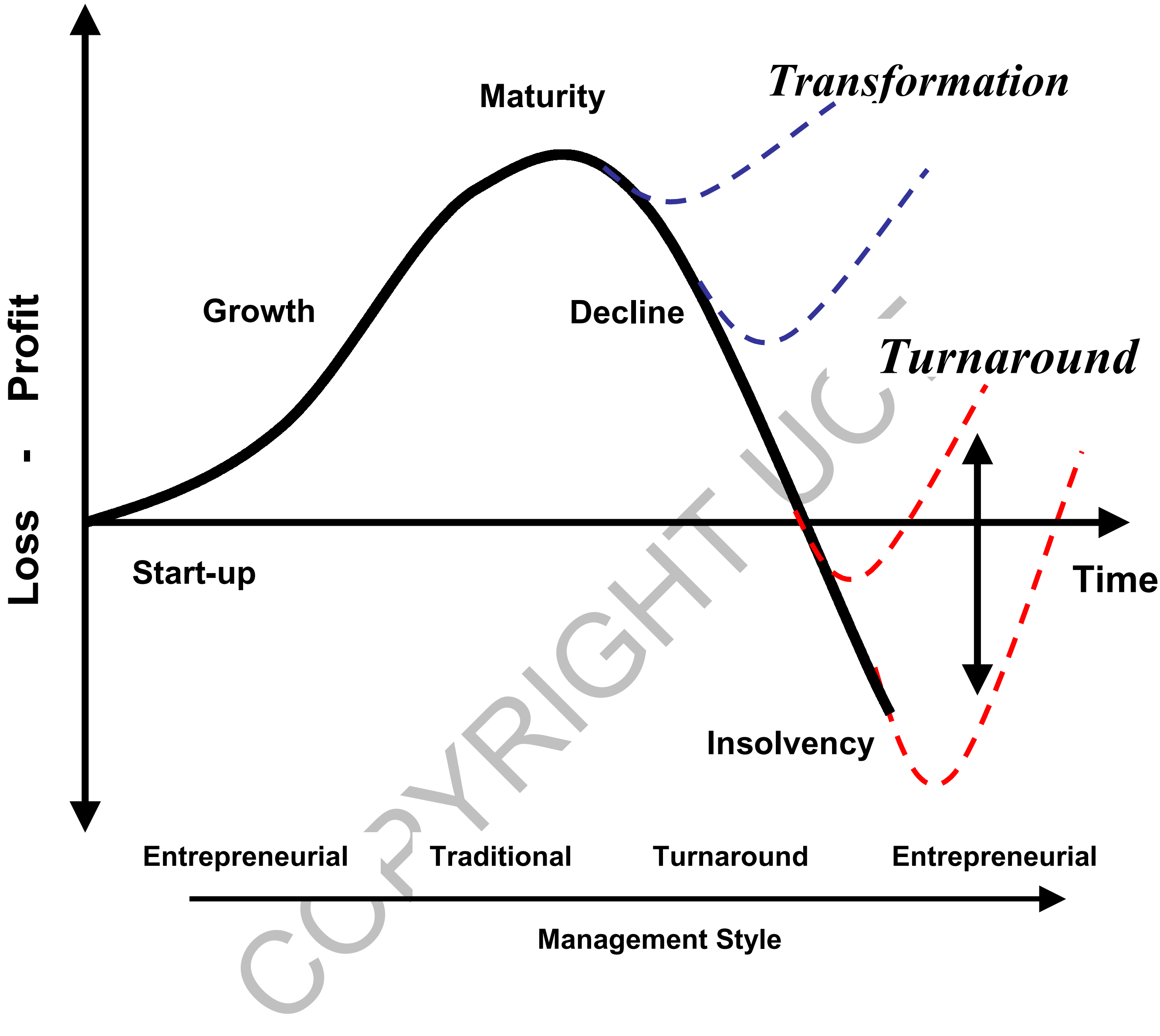
FIGURE A: THE ORGANISATIONAL LIFE CYCLE



Source: Slatter & Lovett, 1999

FIGURE B: TRIGGERS FOR CHANGE IN THE SA AIRLINE INDUSTRY

DEREGULATION

- Lowered the barriers to entry into the domestic market
- New entrants - Flitestar, Phoenix Airways, Sun Air, Comair and Nationwide.
- Introduced greater rivalry in the marketplace.
- New entrants gained market share at the expense of the incumbent SAA.
- Price wars between 1995 and 1998
  - Benefited consumers and led to growth in the domestic market
  - Destroyed the profitability of both new entrants and the incumbent.
  - Flitestar ceased operations in 1994, Phoenix Airways in 1995 and Sun Air in 1999.
  - SAA suffered severe losses, due to lost revenues and costly price wars to regain lost market share.
- By 2000, three players remained - SAA, Comair and Nationwide.

RE-ENTRY INTO GLOBAL COMMUNITY

- Opened up new international markets for SAA.
- Increased competition on international routes
- Increased demand from South African business and leisure customers
- Increased demand from foreigners visiting SA as a tourist destination.

ALLIANCES

- Consolidation in the global airline industry through the formation of code-sharing agreements,
- Led to the formation of alliances between domestic players and global players.
- Alliances formed between Sun Air and Virgin, Comair and BA, Nationwide and Sabena, and SAA and Lufthansa.

FIGURE C: GENERIC SYMPTOMS OF DECLINE

Observer	Business	Capital Markets	Financial Information
General Public	▪ Subject of takeover bid ▪ Obsolete or hopeless products	▪ Very public refinancing	▪ Serious profit warning ▪ Very poor financial results
Informed reader /shareholder	▪ Rapid senior management turnover ▪ Public disagreement among directors over strategy ▪ Repeated failure of product launches	▪ Raising debt or equity to fund losses ▪ Vulture funds trading in debt	Declining: ▪ share price ▪ market share ▪ profits ▪ liquidity ▪ debt to equity ratio ▪ sales volume
City analyst	▪ Lack of investment in new technology ▪ Low morale ▪ Loss of key staff ▪ Loss of key customers	▪ Discussion of financial restructuring plans	▪ Destruction of shareholder value
Suppliers and customers	▪ Worsening terms of trade ▪ Late payment of supplier invoices	▪ Negotiations by suppliers with company bankers to support a difficult restructuring plan	
Investigating accountant	▪ 'Analysis paralysis' ▪ Poor working capital management	▪ Worsening bank security	▪ Creative accounting practices
Employees Major management issues can often only be seen by staff.	▪ Emergency board meetings ▪ Management paralysis ▪ Acting in functional isolation		

Source: Slatter and Lovett, 1999.

FIGURE D: GENERIC INTERNAL CAUSES OF DECLINE

INTERNAL CAUSES	FACTORS
Poor management	▪ Autocratic rule ▪ Combined Chairman and Chief Executive ▪ Ineffective Boards of Directors ▪ Ineffective management ▪ Neglect of core business ▪ Lack of management depth
Inadequate financial control	▪ Poorly designed management accounting systems ▪ Management accounting information is poorly understood ▪ Overhead allocation distorts costs ▪ Organisational structure hinders control
Poor working capital management	▪ Cash outlays funded through overdraft
High costs	▪ Cost disadvantages due to management style and organisational structure ▪ Firm's inability to take advantage of economies of scale ▪ Absolute cost disadvantages ▪ Operating inefficiencies
Lack of marketing effort	▪ Ineffective and wasted advertising ▪ Efforts not targeted on key customers and key products ▪ Lack of market research/ knowledge of the customer's buying habits ▪ Poor after-sales service
Overtrading	▪ Focus on sales volume rather than profit or cash
Big projects	▪ Underestimation of costs ▪ Poor project control
Acquistions	▪ Acquisition of 'losers' ▪ Poor post acquisition management
Financial policy	▪ High debt:equity ratio (high gearing) ▪ Conservative financial policy ▪ Use of inappropriate financing sources
Organisational inertia and confusion	▪ Poor leadership ▪ Lack of clearly defined accountabilities ▪ Poorly motivated staff

Figure E: Generic External Causes of Decline

EXTERNAL CAUSES	FACTORS
Government	▪ Regulated environment ▪ Industry protection/ subsidisation
Changes in market demand	▪ Long term decline in demand ▪ Cyclical market decline ▪ Changing pattern of demand
Competition	▪ Price competition ▪ Product competition
Adverse movements in commodity prices	▪ Raw material prices ▪ Interest rates ▪ Foreign currency prices

Source: Slatter and Lovett, 1999.

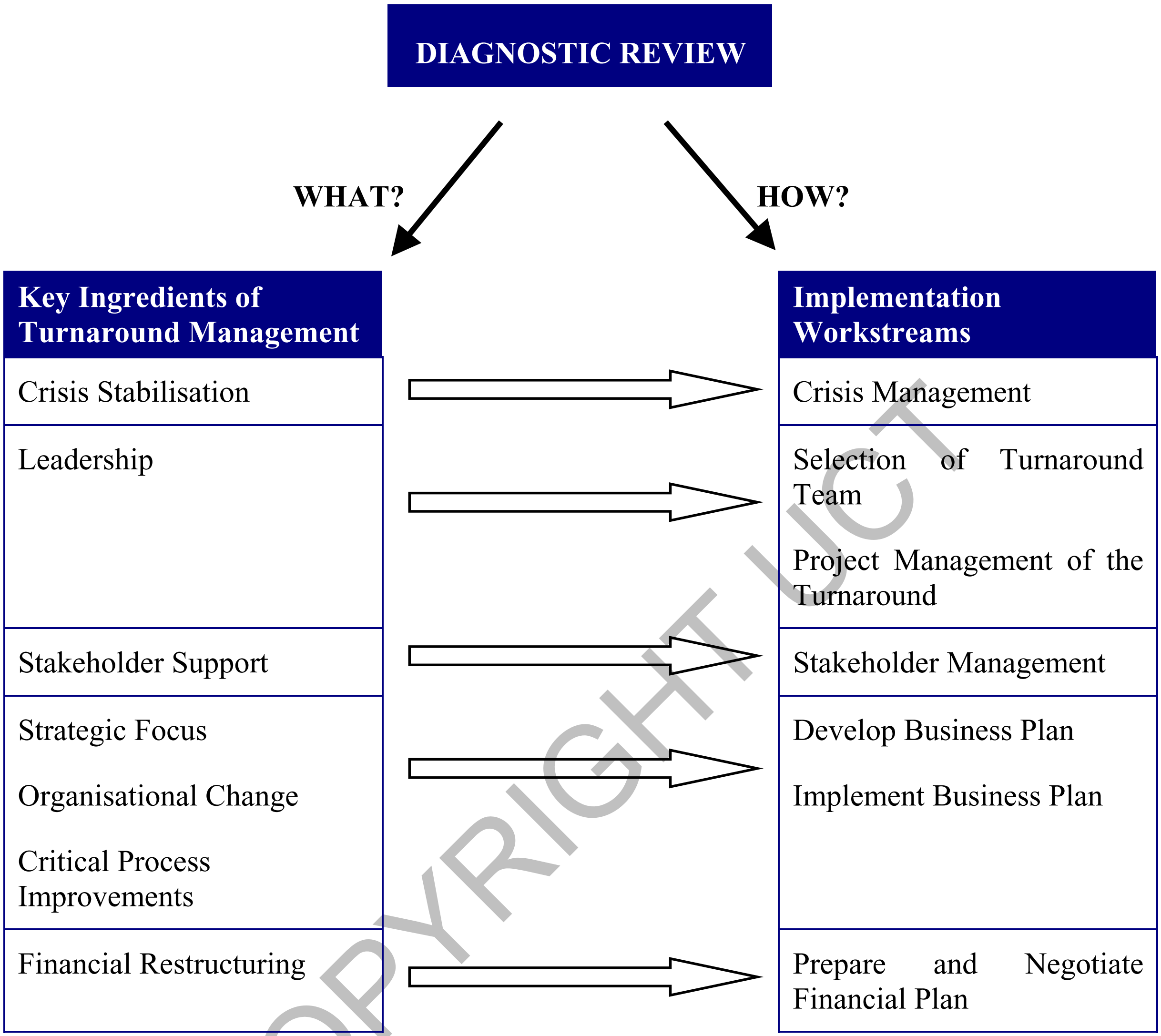
FIGURE F: SAA'S EXTERNAL CAUSES OF DECLINE

EXTERNAL CAUSES	SYMPTOMS
Government:	
▪ International isolation	▪ Insular culture, No best practice
▪ Government interference	▪ Constricted operational and strategic control
▪ Deregulation	▪ Loss of market share, poor profitability
▪ Transition to democracy	▪ Management paralysis
▪ Privatisation policy	▪ Lack of direction and focus
Changes in market demand:	
▪ Poor domestic macro-economic conditions	▪ Lower demand on domestic and international routes, depressed revenues
▪ Asian economic crisis	▪ Lower demand on international routes, depressed revenues
Adverse movements in commodity prices	▪ High input costs for fuel, Low profitability
Competition:	
▪ Domestic	▪ Loss of market share, decline in profits
▪ International	▪ Loss of market share, decline in profits

FIGURE G: SAA'S INTERNAL CAUSES OF DECLINE

INTERNAL CAUSES	SYMPTOMS
Poor management	▪ Lack of real vision, leadership ▪ Lack of strategic focus ▪ Lack of depth and experience in the airline industry ▪ Poor stakeholder management manifested in the tensions between CEO Myburgh and Executive Director and Chairman Nomvete ▪ Inability to engage stakeholders in the privatisation process ▪ Low credibility amongst staff ▪ Poor financial control, Lack of accountability ▪ Poor strategic choices ▪ No sense of urgency ▪ Bureaucratic, Hierarchical, Functional isolation ▪ Poor communication ▪ Paralysis
Inadequate financial control	▪ Inadequate management control systems ▪ Ineffective control. ▪ Information Systems were outdated and inadequate
High costs	▪ High fuel costs and high labour costs - 2 key cost drivers ▪ Poor operating efficiencies ▪ Route networks were not optimal ▪ High purchasing costs
Lack of marketing effort	▪ Lack of market orientation ▪ Did not value customers ▪ Lost market share ▪ Lacked a clear strategic marketing focus ▪ Marketing efforts were uncoordinated
Organisational inertia and confusion	▪ Low productivity and low staff morale ▪ No sense of urgency ▪ No clear direction from the top management

FIGURE H: KEY INGREDIENTS AND WORKSTREAMS



Source: Slatter and Lovett, 1999.

FIGURE I: THE TURNAROUND IMPLEMENTATION PHASES

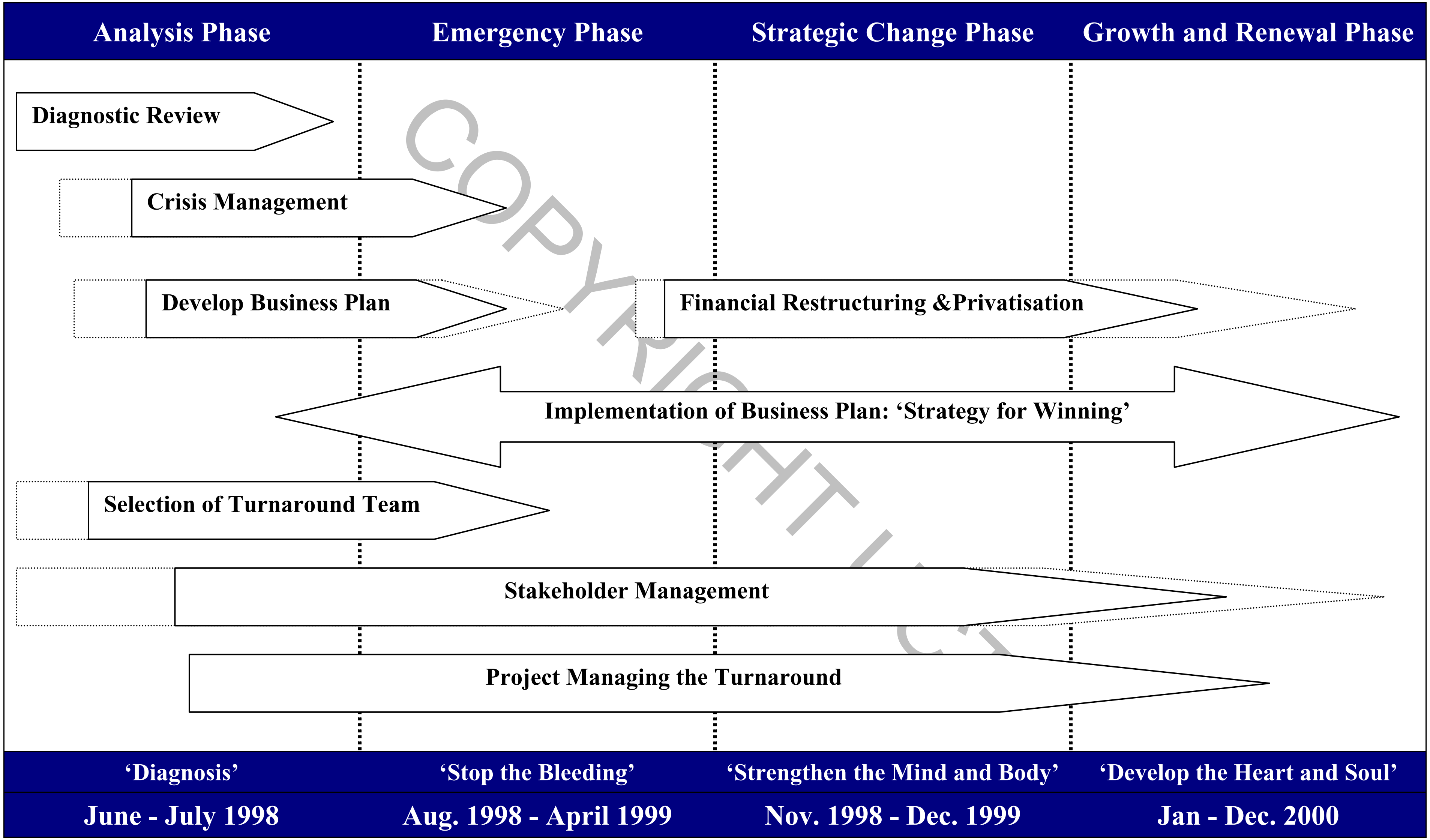


FIGURE J: SAA TURNAROUND 'STRATEGY FOR WINNING' KEY ACTION STEPS

DATE	Customer Service	Revenue Management	Cost Reduction	Alliances	Fleet Upgrade	Transform Staff	New first and business class product
June '98	Market Research						
July '98	Most common complaint - late flights				1 x B747-400 delivered		
Aug. '98	Go quiet on marketing	Restructure national sales team				Re-design HR dept.	
	Set on time Performance targets	Key Account Travel Management				Re-design flatter organisational structure	
	Incentivise staff	Bring in RM experts				Introduce incentives	
Sep. '98	Launch 2-part marketing campaign	Train employees			Cancel B777 order and order 2 more B747's	Focus on teamwork	
	1: Listen to customers	Acquire revenue management software					
Oct. '98	Improve on time performance	Intensify price war		Sign code-share agreements with Lufthansa, Swissair and Singapore Airlines			
Nov. '98			Retrench staff		1 x B747-400 delivered		

DATE	Customer Service	Revenue Management	Cost Reduction	Alliances	Fleet Upgrade	Transform Staff	New first and business class product
Dec '98	2: Tell customers about achievements		Terminate loss-making int'l routes		2 x B747-400 delivered		
Jan. '99	Reward staff		Purchase savings: R22m			Establish Transformation Consultative Forum	
March '99		New Call Centre	Restructure international commissions: R34m saving				
			Re-focus technical services and maintenance: R120m saving			Leadership development programme	
Aug. '99	Retrain frontline staff	Reviewed Cargo operational strategies	Fewer org. levels				
	Recruit new cadre of flight attendants		Optimise cargo routes: R80m saving				
Oct. '99		Focus on top 20-30 local cargo customers	Outsource IT systems saves R90m	Sign code-share agreement with Delta			Announce R800m spend on new products
Feb. '00			Sign agreement with Atraxis		Order 21 new B737-800's	Intake of 20 Cadet Pilots	

DATE	Customer Service	Revenue Management	Cost Reduction	Alliances	Fleet Upgrade	Transform Staff	New first and business class product
March ‘00			Purchase savings: R140m				
June ‘00			Improved asset utilisation		Re-organise and corporatise Technical Division		Launch 1st class lounge at Jhb. Int’l
July ‘00					3 x B737-800’s delivered		Launch of ‘kerbside’ check-in
Nov. ‘00				Code-share agreement with Qantas			Further staff training

THE TURNAROUND OF SOUTH AFRICAN AIRWAYS: 1998 - 2000

SECTION 3: THEORETICAL OVERVIEW

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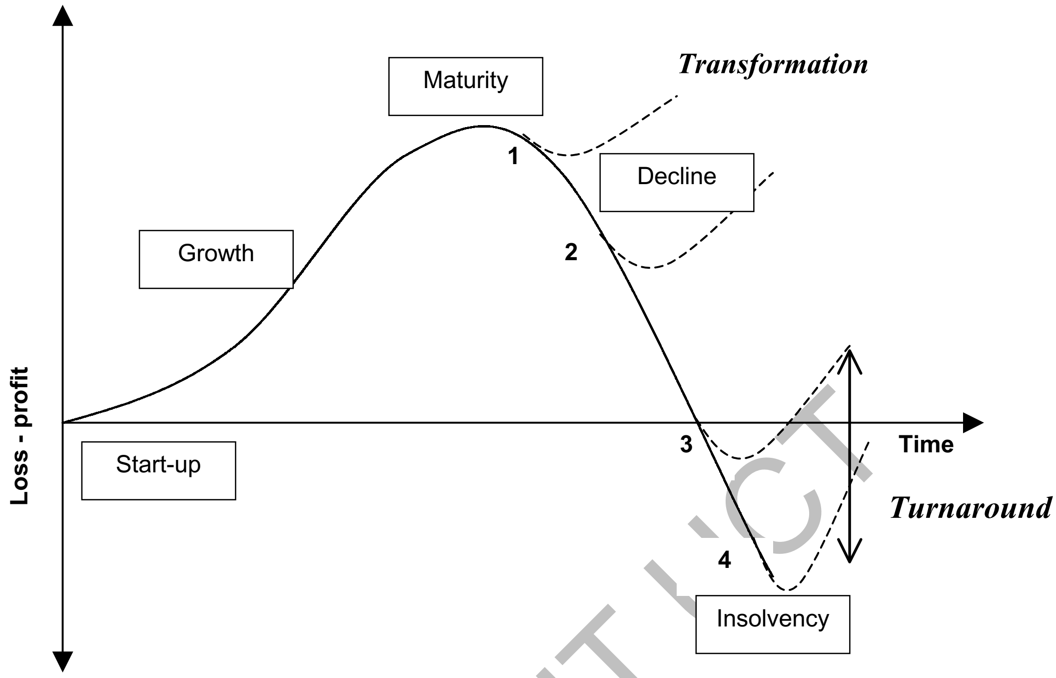
Definition of Turnaround

A starting point for most of the literature is the defining of a turnaround situation. Slatter and Lovett (1999:1) use the term to refer to 'those firms whose financial performance indicates that the firm will fail in the foreseeable future unless short-term corrective action is taken'. Bibeault (1982:2) views a turnaround situation as one in which 'a firm suffers from excessive liquidation problems'.

Slatter and Lovett do not limit their definition of a turnaround situation to companies with a cash crisis. Whenever there is a cash crisis there is a turnaround situation, but the company need not have a current cash crisis. They suggest a broader definition which includes stagnant businesses with under-utilised assets and ineffective management. Many such firms survive in spite of poor management. A growth-oriented firm that has grown too fast may continue to be quite profitable while at the same time being in a severe cash crisis. A typical sign of a turnaround situation is a trend of successively lower profits culminating in a loss situation and a cash flow crisis. In terms of an organisational lifecycle perspective, after reaching maturity, all points of decline except point 1 (see Figure I) may be considered as candidates for a turnaround management strategy.

A turnaround should be distinguished from a transformation, a workout and an insolvency. Turnarounds seek to achieve sustained viability fast whereas transformation projects aim to achieve a high level of absolute and relative performance improvement over the medium term and do not encompass crisis management, capital restructuring or dealing with stakeholders. A workout describes a creditor-led process to avoid insolvency. A turnaround is debtor-led and involves a greater emphasis on business improvement. The objective of the turnaround is the rescue of the company, not its liquidation. Therefore, only management can lead the rescue of a troubled company; investors and debt providers cannot lead the process. Insolvency allows for limited protection for creditors to develop a rescue plan, or provides for the realisation of a company's assets and the distribution to its creditors (Slatter and Lovett, 1999:7).

Figure I: The Corporate Life Cycle



Source: Slatter & Lovett, 1999

Symptoms and Causes of Decline

Symptoms

Corporate decline can be identified by a number of early warning signals such as declining margins, declining percentage of market share, declining working capital, rapid increase of debt, and low morale of staff (Bibeault, 1982:61). Slatter and Lovett (1999:13) point out that it is important to distinguish between symptoms and causes of decline or failure. They argue that symptoms might give clues as to what is wrong with a firm, but that they do not provide a guideline for management action. They use the analogy of a sick patient to describe the condition of a firm requiring a turnaround approach. In order to help the 'sick' firm recover it is important to find the root causes of the firm's problems. For example, a headache and temperature may be the symptoms of an illness, but a doctor will have to find the causes of these symptoms to correctly treat the patient. An important distinction between a sick patient and a dying company, however, is that the latter requires the support of the stakeholders around it to survive. It is therefore sometimes necessary to treat the publicly visible symptoms so as to restore confidence and build support.

Slatter and Lovett argue that observation of the different symptoms of a company entering decline depends on the observer's *perspective*. Those closest to the company are usually able to see the onset of problems before outsiders, who tend to rely on publicly available financial information to analyse the company's performance. There are many non-financial symptoms of decline which act as important warning signs before the financial symptoms manifest themselves, and it is critical that these are identified and acted upon early. By the time that the financial impact of the causes of decline reveals itself it may be too late to save the company. They present a framework of the more common symptoms of decline from different observer perspectives. The perspectives that they list include the 'man in the street', the informed reader/shareholder, the city analyst, suppliers and customers, the investigating accountant and employees. The symptoms are found within the business itself, the financial information available on the company or in the capital markets. Table I summarises some of the most common symptoms of failure

Table I: Symptoms of Decline

Within the Business	**Financial Information**
Subject of takeover bid	Serious profit warning
Rapid senior management turnover	Very poor financial results
Obsolete or hopeless products	Declining share price
Public disagreement among directors over strategy	Destruction of shareholder value
Repeated failure of product launches	Creative accounting practices
Lack of investment in new technology	Declining liquidity
Low morale	Declining sales volume
Loss of key staff	High debt to equity ratio
Loss of key customers	Declining market share
Worsening terms of trade	Declining profits
Late payment of supplier invoices	**Capital Markets**
'Analysis paralysis'	Very public refinancing
Poor working capital management	Raising debt or equity to fund losses
Emergency board meetings	Vulture funds trading in debt
Management paralysis	Discussion of financial restructuring plans
Acting in functional isolation	Worsening bank security

Source: Slatter and Lovett, 1999

Some of these symptoms of decline are present in healthy companies, but it is usually a combination or 'cocktail' of symptoms and the observation of a trend over time that should warn management and stakeholders of impending problems.

The Altman Z score can also be used as a good predictor of company failure (Bibeault, 1982:63). Edward I. Altman of the Graduate school of Business of New York University, developed the Z score which is designed to forecast failure in the short term. It uses ratios of management ability and financial strength to arrive at a Z score where:

$$Z = 1.2x_1 + 1.4x_2 + 3.3x_3 + 0.6x_4 + 1.0x_5$$

and:

- x_1 = working capital / total assets
- x_2 = retained earnings / total assets
- x_3 = EBIT / total assets
- x_4 = market value of equity / book value of debt
- x_5 = sales / total assets

Slatter and Lovett point out that the Z-score has been found not to be a predictor for longer than two years before bankruptcy, which therefore limits its use as there are more conventional techniques to predict failure this early on. They quote Tafler whose study concluded that financial gearing and profitability measures were the most significant ratios in predicting failure.

Causes

In terms of the causes of corporate decline after firms reach maturity there are both external reasons, such as changes in the economic climate, competitive change, government constraints, social changes and technological changes, as well as internal reasons. External reasons can be divided into external changes and external constraints. The difference between the two lies in their degree of severity. Constraints, such as government constraints block management action and are therefore more difficult to overcome than changes such as economic, social or technological. Bibeault (1982:25), referring to a survey of CEO's, attributes external factors as the sole cause in 9% of the cases of corporate decline. On the other hand in 70% of the cases of corporate decline, the causes can be traced to internal factors. Where the decline is traced to internal factors, management is the principal reason 85% of the time. Table II shows the principal reasons for corporate decline that Bibeault found in his survey.

Table II: The Principal Reasons for Corporate Decline

Reason	Percentage
Sheer bad luck (Dun & Bradstreet 1977)	1%
External factors beyond management's control	8%
Real balance of external and internal factors	24%
Internal problems triggered by external factors	15%
Internally generated problems within management's control	52%

Source: Donald B. Bibeault, Survey of Eighty-One Turnaround Company Chief Executives, April 1978.

Slatter and Lovett (1999) observe that it is possible to argue that almost all the reasons for declining performance can be traced back to 'bad management' even where the original causes are in the external environment and management has not responded effectively to them. They warn that this approach, which was common in the 1980's, is simplistic and that while it locates the blame for a firm's decline, it fails to provide those charged with leading the recovery with any useful analytical information. If it were simply a case of bad management, then the solution would simply be to change the management. This is, however, really only one step in the process of turning a failing company around.

A deeper analysis of the causes of decline reveals a 'chicken and egg' phenomenon. For example, intense price competition in the marketplace may be identified as a causal factor of decline. But this may have been caused by a firm's inferior cost position relative to that of its competitors, and this in turn may have been caused by a lack of market share or conservative financial policies, or both. If financial policy is identified, then this would again lead to 'bad management' being the root cause. In this way, one may be able to identify a *chain* of interrelated causal factors. Slatter and Lovett separate the causes of decline into internal and external causes. They identify ten principal internal causes and three external causes of decline, as shown in Table III.

Table III: Causes of Corporate Decline

Internal Causes	External Causes
Poor management	Changes in market demand
Inadequate financial control	Competition
Poor working capital management	Adverse movements in commodity prices
High costs	
Lack of marketing effort	
Overtrading	
Big projects	
Acquisitions	
Financial policy	
Organisational inertia and confusion	

Source: Slatter and Lovett, 1999.

Characteristics of Turnaround Management

Slatter and Lovett (1999) suggest that it is worth distinguishing between firms that survive but never make adequate returns on capital employed, or survive only in the short-term and then become insolvent, and those which achieve sustainable recovery. The latter involves achieving a viable and defensible business strategy, supported by an adequate organisation and control structure. Sustainable recovery requires the firm to develop sustainable competitive advantage. There are three main sources of competitive advantage for the firm to exploit: economic factors, organisational factors, and political and legal factors. Economic factors provide three sources: absolute cost advantage, relative cost advantage and product differentiation. Organisational factors relate to the quality and expertise of management which in turn affect the quality of strategy implementation. Political and legal factors may provide firms with advantage against its competitors. An example of this would be the subsidisation of state-owned enterprises and the favouring of domestic firms over foreign competitors.

A corporate turnaround according to Bibeault (1982:81) is a substantial and sustained positive change in the performance of a business. Companies that have had several years of declining profits or even substantial losses use turnaround to break out of the declining performance. In these turnaround situations change is a characteristic and this often includes the appointment of a new CEO, be it an internal or external appointment. Brege and Brandes (Hussey, 1996:145), consider the appointment of a new CEO as the starting point of the turnaround. Their research points to the need for an external appointment for the process to be successful. Dunlap (1996) adds that for the most part companies cannot fix themselves solely from the inside since management have vested interests. He says if the correction is too painful managers won't have the backbone to do it. He therefore also suggests a catalyst such as a new executive or manager brought in from the outside.

Turnaround management for Slatter and Lovett (1999) is holistic and must address both strategic and operational issues. Rescue plans must seek to cut costs and grow revenues. The perspective must be both short term and long term. Characteristics of the appropriate remedy for a rescue plan or turnaround for Slatter and Lovett should: address the fundamental problems, tackle the underlying causes (rather than symptoms), and be broad and deep enough in scope to resolve all the key issues.

There are broadly 3 types of operating turnaround strategies: cost cutting, revenue generating and asset reduction. The decision on which strategy to choose is based on cash flow projections and cash flow break even charts. (Bibeault, 1982:226).

There is no one particular turnaround formula because circumstances differ and approaches vary. Bibeault (1982:85) lists 5 principle types of turnarounds:

- the management process turnaround
- the economic or business cycle turnaround
- the competitive environment turnaround
- the product breakthrough turnaround
- the government related turnaround.

Linked to his finding that management is the principal internal reason for decline, management process turnaround corrects the management weaknesses that caused the decline.

Phases in the Turnaround Process

Slatter and Lovett (1999:5) suggest four phases that the organisation will go through during a turnaround:

- Analysis phase
- Emergency phase
- Strategic change phase
- Growth phase

Bibeault (1982:92) breaks the turnaround into five stages. These stages are similar to those of Slatter and Lovett but include an additional initial phase; the management of change stage. This stage is where the company realises it has major problems and decides to do something about them. The next four stages, evaluation stage, emergency stage, stabilisation stage and the return to normal growth stage are comparable to those of Slatter and Lovett as above.

According to Slatter & Lovett (1999:6) there are four main objectives that need to be addressed by the CEO:

- Take control and manage the immediate crisis
- Rebuild stakeholder support
- Fix the business
- Resolve future funding

Within the four stages of the turnaround process and the four objectives given above, Slatter & Lovett identify seven essential ingredients for a successful turnaround:

- Crisis stabilisation
- Leadership
- Stakeholder management
- Strategic focus
- Organisational change
- Critical process improvements
- Financial restructuring

There is an overlap between these seven essential ingredients and the four key steps to a successful turnaround identified by Dunlap (1996):

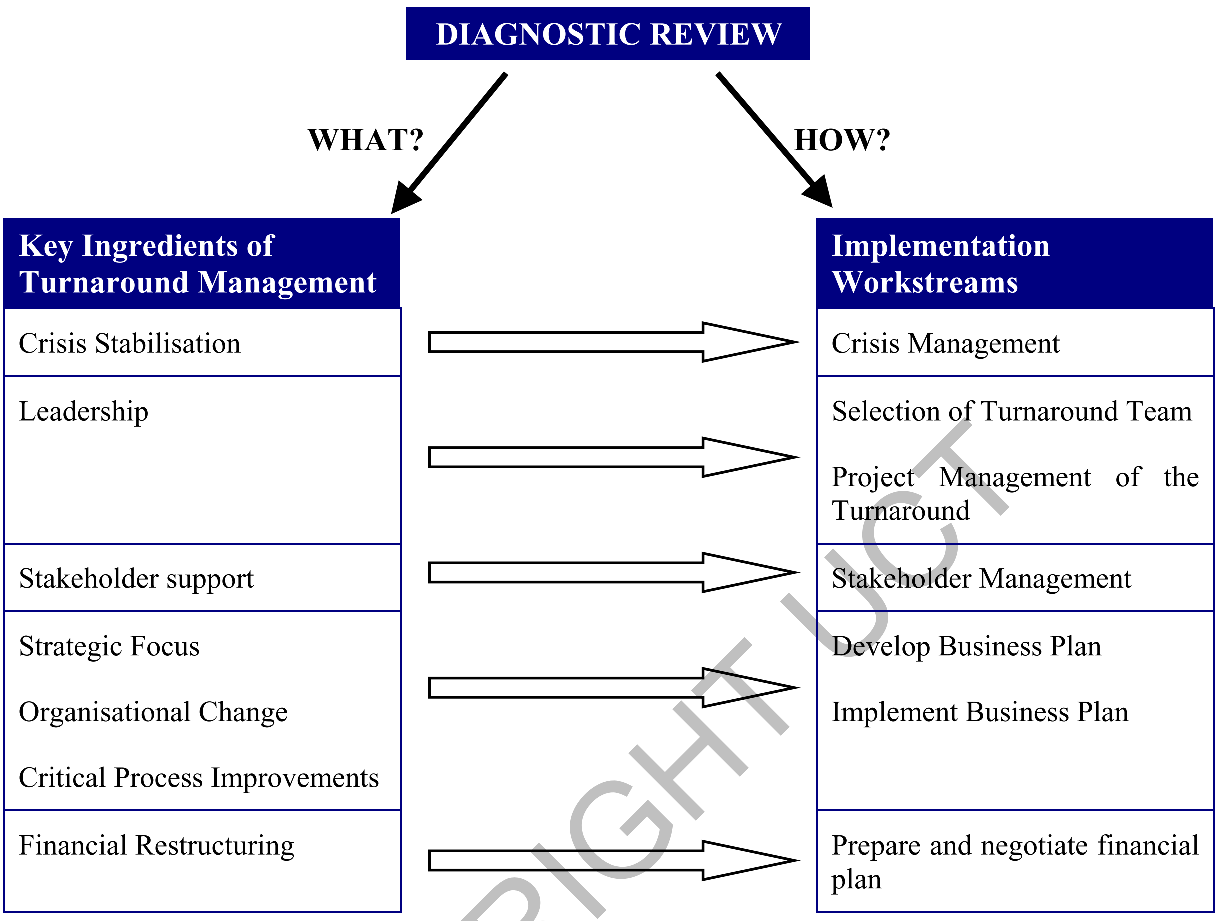
- Get the right management team ('Magnify your own abilities by surrounding yourself with great people')
- Cut back to the lowest costs ('Cost is always your enemy')
- Improve the balance sheet ('Focus like a laser')
- Get a real strategy ('Envision the future and plan a route to it')

Implementation Framework

Slatter and Lovett (1999:75) have developed an approach that together with their seven essential ingredients for turnaround has an implementation framework consisting of seven key workstreams. They argue that a successful turnaround depends upon developing an appropriate turnaround prescription and an effective implementation. While the first point addresses what needs to be done the second point addresses how it should be done. The starting point is thus a diagnostic review to establish the true position of the troubled company and to determine whether a turnaround – as opposed to insolvency, immediate sale or liquidation – is a viable option. Slatter and Lovett refer to the seven implementation processes as workstreams. These workstreams are the essential implementation tasks of the turnaround. The link between the key ingredients and the implementation workstreams is illustrated in Figure II.

The first step of crisis stabilisation is implemented by taking control of the distressed business and instituting aggressive cash management. Appointment of a Chief Executive to lead the turnaround and the selection of his/her team is next. For effective leadership it is also necessary to ensure project management of the whole turnaround process. In order to gain stakeholder support it is necessary to rebuild stakeholder confidence and reconcile the different interests within the overall recovery plan. In terms of strategic focus, organisational change and critical process improvements, Slatter and Lovett suggest that a business plan is developed and implemented. The last of the seven key ingredients, financial restructuring, is achieved by restructuring the capital base and raising the money to fund the turnaround. The turnaround process is characterised by considerable overlap of the planning and implementation phases. The workstreams are phased throughout the four phases, analysis, emergency, strategic change and the growth phase of the turnaround process.

Figure II: Key Ingredients and Workstreams



Source: Slatter and Lovett, 1999.

Drivers for Turnaround Management

Political change, macro-economic conditions, and industry competition are three drivers of demand for turnaround management (Slatter and Lovett, 1999:9). Radical political change creates a demand in transitional economies. The moves towards a market economy and mass privatisation have put pressure on state-owned enterprises to reform or die. In many of such cases the scale and urgency of the restructuring required mean that the change programmes are genuine turnarounds rather than business transformation.

Practical Literature Review

Turnaround specialists such as Bethune and Dunlap, who have written about their experiences of turning companies around, provide a source of practical literature which supplements the theoretical literature. Bethune's experience relates to the turnaround of an airline, Continental. He paints a picture of an airline in serious crisis when he joined the company in 1994, with the worst performance in relation to its competitors with regard to service and customer satisfaction (Bethune and Huler, 1998). Labour relations were poor and employee morale low. The share price was at a low of $3.25 and the firm faced a cash crisis. Within less than a year Bethune turned Continental around from a loss of $204 million to a profit of $202 million. After posting eleven successive quarters of record profits, by 1996 their stock was regularly trading at more than $50. In early 1997, Air Transport World the industry's leading monthly, voted Continental 1996 Airline of the year.

Bethune identifies his key actions in turning Continental around. His starting point in dealing with the situation was to get all stakeholders to question what the problems were and who should take ownership of them. Then he developed a 'Go Forward Plan', which addressed not only the marketing and financial problems but also the underlying causes of the problems. His first step was to cut back on costs, to take control of the finances by eliminating functions that were losing money and renegotiating loans and leases. Next he focussed on what the customers wanted. They measured what was most important to the customers and incentivised the staff to achieve goals linked to these measures. He insisted on open lines of communication and a sharing of information with staff (both good and bad news). Key to their success was that everyone knew the main goal, winning, and that they worked together as a team to achieve it. His approach was also one of balance with a recognition of the inter-relation between marketing, finance, the product and employee morale. None of these could be addressed alone.

Bethune gives one final reason for their success. He says that *"We at Continental have learned the secret to winning. If you want to lead, you have to follow. If you want to command, you have to serve"* (Bethune and Huler,1998:281).

Leadership style

For a turnaround to be successful the management team must have the capabilities, motivation and initiative to bring about positive change (Slatter and Lovett.1999:120). In assessing whether or not the management team have the capability to implement the required strategies to effect change it is important to look for certain characteristics. In particular, characteristics pertaining to style and approach may be more relevant than specific business or industry experience.

Dunlap (1996) says a business leader needs an inner circle; a management or operating committee. According to him, it is important that the management team is a general reflection of the leader, without being carbon copies. He adds that it is important that they challenge the leader and bring ideas to the company. When looking for a team it is useful for a Chief Executive Officer (CEO) to recruit people who have worked with him/her before and also who have been through change. Dunlap also points out that in every company there are some competent people who are buried by layers of corporate politics and bureaucracy and that by removing the shackles of bureaucracy these people can then flourish.

In terms of leadership in a turnaround Bibeault (1982:149) identifies three main aspects. First, the turnaround leader is the architect of the turnaround strategy, second, he/she is an implementer of strategy, and third, the turnaround leader is a personal leader. The leader is a personal leader in that he/she is someone distinctive from all other persons in the organisation. According to Bibeault, how the leader's personal style contributes to company performance, character and tone is more important in turnaround than at any other time in corporate life.

For Bibeault the aspect of leadership in turnaround is the most important where the turnaround leader is an implementer of strategy. The leader must supply the organisational strategy and promote and defend it. Where necessary the leader must integrate the conflicting interests and ensure that the organisation's essential needs are met. Finally the leader must be the judge of the results.

There is no one given executive style to turnaround leaders and Bibeault (1982:150) says that there is not necessarily a consistency in the styles of approach. He argues that there is however a consistency in the pursuit of the objectives of turnaround leaders. While it is difficult to generalise about their characteristics, Bibeault identifies four required skills from his contact with turnaround leaders:

- an entrepreneurial instinct coupled with professional management skills
- broad business experience
- expert negotiating skills
- expert interviewing skills

Negotiating skills is one of the key abilities for a turnaround leader since he/she is usually faced with lender and board pressure when approaching a turnaround assignment. The lender negotiations can be critical to the eventual success. In addition these negotiation skills are crucial in labour union discussions, and supplier and creditor contract agreements.

Kotter (1992) adds the dimension of managing cultural change within the organisation and argues that for a leader to successfully manage this change there are three characteristics that are needed: the leader should be effective, have an outsider's perspective, and an insider's resources. Kotter notes that leadership from one or two people at the very top of the organisation seems to be an absolutely essential ingredient when major cultural change occurs. He relates this firstly to the sheer difficulty of changing cultures and the power it requires (this power usually resides at the top of the hierarchy). Secondly the interdependence inside organisations can make it difficult to change anything significantly without changing everything related to it. The establishment of a strong leadership process to supplement the management process is also an essential part of major cultural change in an organisation.

Kotter (1990:6) distinguishes between management and leadership. Leadership for Kotter is establishing direction, aligning people, motivating and inspiring, and producing change. The leader develops a vision of the future and the strategies for producing the changes needed to achieve the vision. He contrasts this with the management role of planning and budgeting, where detailed steps and time frames are established, and the managers then allocate the necessary resources. According to Kotter, leadership often entails producing change to a dramatic degree, while management produces a degree of predictability and order.

Westley and Mintzberg (1989) present a number of typologies of visionary leadership, namely the creator, the idealist, the bricoleur, the proselytiser and the diviner, to indicate the possibilities for variations in visionary style. The creator is characterised by the originality of his or her ideas and the holistic quality of their realisation, while the idealist speculates on an ideal. In contrast to the creator and to some extent the idealist, the bricoleur's genius resides in an interactive, social ability to 'read' situations and recognise the essential insight. The proselytiser is the most dependent of the five visionary styles. While creators rely on others to enact their vision, proselytisers depend on others to stimulate their vision. The salient capacity of the diviner is insight, which comes with great clarity in moments of inspiration. In this respect the diviner is like the creator but differs in that the diviner tends to focus on process as opposed to product. They conclude that strategic vision is part style, part process, part content and part context. Visionary leadership according to Westley and Mintzberg involves psychological gifts, sociological dynamics and the luck of timing. Their research also indicates that visionary leaders are products of their environments, and that as times and contexts change so the visionaries of yesterday fade into obscurity. They also emphasise that visionary leadership is not always synonymous with good leadership. Westley and Mintzberg see the idealist and bricoleur as being well suited to turnaround situations.

Slatter and Lovett (1999:156) acknowledge that it is unusual to find all the required qualities for a turnaround manager in one person. An ideal turnaround manager will be both a strong leader and a good manager. They suggest an approach of building a turnaround team that has the blend of skills required for the different stages of the turnaround process.

An ideal person and/or team, Slatter and Lovett suggest, would have:

- considerable leadership skills
- flexibility, and the ability to listen and modify views
- the ability and courage to make rapid decisions based on a minimum of data and analysis; be analytical and able to prioritise quickly
- the ability to balance short-term vision and longer-term vision
- the courage to take unpopular decisions
- high integrity
- confidence in his/her own abilities
- experience at driving through change in difficult times
- entrepreneurial instincts – uncomfortable with the status quo.

The turnaround manager must be action-oriented and focused. He/she should also be able to overcome the politics of the organisation. An ability to evaluate management and operations and think clearly and with common sense is also necessary. The ability to inspire confidence and reassure people as well as to instil standards and discipline throughout the organisation are also characteristics of the turnaround manager.

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