

## LEARNING FROM CRISES: A LOST OPPORTUNITY?

Drago Dubrovski  
International School for Social and Business Studies, Slovenia  
linnair@siol.net

### **Abstract:**

All crises create a distressing, uncertain and worrisome situation, which endangers property as well as people and influences established business and life flows. The extent of the crisis is simultaneously reflected in several areas, making it a complex or multidimensional phenomenon, affecting the economic, social, traditional, psychological and legal aspect. On the other hand, a crisis also initiates and directs the renewal of the company. In view of the complexity of the management of a company undergoing serious difficulties, crisis management is therefore denoted as a “composite” discipline, because a multi-disciplinary approach to problem solving is required in order to achieve the objectives of managing a company undergoing a crisis. However, empirical evidence from the author’s research has shown that companies in acute crisis extremely rarely present changes to the business model that would replace previous ineffective business practices that led to the acute crisis and focus mostly on the consequences of their crisis and the measures of short-term financial disburdening, which provides no guarantee to the participants that the crisis in these companies will actually be solved even for a mid-term time period.

*Keywords: crisis, crisis management, radical change, business model*

## 1. INTRODUCTION

In everyday reports, various more or less expert studies, and as well as corporate and other organizational sources, we often encounter statements on natural disasters, a variety of conflicts, major or minor problems that companies are facing, or are even compulsorily dissolved, an alarming decline in the performance of individual industrial or services sectors, and even countries which are associated with the notion of crisis in one way or another. The crisis is quite often used to mark uncertain, difficult, and dangerous or crucial situations for the future, as it refers to an extremely wide field of natural, social, economic and mental processes (e.g. a political crisis, economic crisis, financial crisis, oil crisis, ecological crisis, moral crisis, crisis of the arts, crisis of values, health crisis, mid-life crisis, etc.). In everyday language, the crisis has most often a negative connotation, because it is associated with a variety of inconveniences, difficulties and threats. Especially in more recent times, this term and phenomenon has become “popular” in everyday communication from the second half of 2008 onwards, when virtually the whole world became involved in the first financial crisis (problems in the financial sector and a drastic decline in the value of investments), and then also the economic crisis (problems of the real sector).

All crises create a distressing, uncertain and worrisome situation, which endangers property as well as people, and influences established business and life flows, which is why we want to resolve this situation as soon as possible. Crises in the wider socio-economic environment directly or indirectly affect the position of individual companies or other organizations which may be more or less connected with the broader scope of the crisis. A crisis in one sector (e.g. automotive, construction etc.) may have a significant negative impact on the companies from completely different sectors. A crisis can impact any company (Crandall & Mensah, 2008) even if at a certain time the company is efficient in a fast-growing and, according to all criteria, a high-potential industry, as the crisis can be caused by reasons which are not directly connected to the same industry. The life cycle of a business and the industry in which it operates can be very different. There are countless examples of global companies in domestic and foreign business history, which seemed indestructible in their peak but are actually gone today.

## 2. CRISIS AS A MULTI-ASPECT PHENOMENON

The extent of the crisis is simultaneously reflected in several areas, making it a complex or multidimensional phenomenon, affecting the economic, social, traditional, psychological and legal aspect (Table 1). A crisis is a short-term undesired, unfavourable and critical situation in a company (organization), directly endangering the existence and further development of this organization and is caused by an intertwined and simultaneous action of both external and internal sources (Dubrovski, 2004; Dubrovski, 2011, p. 31; cf. also Barnett & Pratt, 2000; Barton, 1993; Crone, 2007; Fink, 1986; Grünert, 2007, p. 9; Heath, 1998; Hermann, 2008, p. 211; Homel, Knecht & Wohlenberg, 2006, p. 33; James & Wooten, 2010, p. 17; Kraus & Becker-Kolle, 2004; Lalonde, 2008, p. 24; Lerbinger, 1997; Neubauer, 1999, p. 8; Roux-Dufort, 2003, p. 51; Slatter, 1987).

**Table 1:** The dimension of a crisis – crisis as a multi-aspect phenomenon

Aspect of the crisis	Content
The economic aspect	<ul style="list-style-type: none"> <li>• endangers property as well as people and influences established business and life flows,</li> <li>• redistributes the positions of market participants,</li> <li>• changes the principles of success and increases the threshold requirements for survival.</li> </ul>
The social aspect	<ul style="list-style-type: none"> <li>• changes the behaviour of the participants in the crisis,</li> <li>• redistributes the positions of individuals and certain groups in society,</li> <li>• and increases the proportion of individuals below the threshold of economic and social risks.</li> </ul>
The traditional aspect	<ul style="list-style-type: none"> <li>• brings a break with previous practices – i.e. business models, structures, processes, systems, strategies and culture – and starts a new business life cycle of the organization,</li> <li>• new foundations for the construction of the core capabilities of the organization and competition factors are required,</li> </ul>

	<ul style="list-style-type: none"> <li>• and it brings new management ideologies and approaches.</li> </ul>
The psychological aspect	<ul style="list-style-type: none"> <li>• promotes a state of tension and conflicts between the participants of the organization, worry, stress and uncertainty,</li> <li>• promoting the culmination of problems of the organization with only two possible solutions – the ruin or survival, resulting in a change in the “psychological profile” of the organization and its members,</li> <li>• incidence of disease symptoms of the organization and its members.</li> </ul>
The legal aspect	<ul style="list-style-type: none"> <li>• requires a greater consideration of additional specialized laws and implemented policies, primarily of obligation, equity and insolvency law,</li> <li>• a more strict compensation and social responsibility of the management,</li> <li>• draws the functioning of the organization closer to the edge of legality and legitimacy.</li> </ul>

The crisis may also affect non-profit institutions and organizations (companies). Also societies, schools, hospitals, sports clubs, churches, state institutions, city or local communities etc. are facing the crisis, where it is basically the same definition of a crisis, however the causes, consequences and ways of solving the crisis may differ with regard to business organizations. In this area, Spillan (2003) distinguishes between the following categories of “critical events”: executive crisis (e.g. problems in the computer system), problems with the public (accidents related to the activity or product with a negative impact on the public), unethical behaviour (fraud, espionage, campaigns, theft, workplace violence, etc.), natural disasters (floods, storms, earthquakes etc.), and legal crises (compensation, investigations, lawsuits etc.). Researches (Parnell, Koseoglu & Spillan, 2010) show that governments are much less successful agencies in addressing crises than private institutions.

In terms of the management of the company or strategic business decision makers, crisis brings exceptional situations, which require very rapid decision-making due to the critical state of the moment, and these decisions must be as correct as possible, as usually adjustments are not possible, therefore the crisis also contains a managerial viewpoint. Emergency situations represent a situation in which it is not possible to use tried and tested routine decisions, as the company is facing these new situations (at least in this way) for the first time. The timing and decision-making pressure is in contrast with the causes and the course of the emergence of the crisis, which is usually a long-term process. The management of the company is therefore directly confronted with the characteristics of emergency situations that require a different approach by the company’s management, as opposed to normal conditions.

Part of the characteristics of the company in crisis is general, so it accompanies all sorts of crises, but with different intensity. The second, and more extensive part, which is also crucial for the strategic and tactical dealing with crisis situations, is special and varies from case to case. Namely it is not possible to ignore the fact that every company despite being a part of a common industrial or service sector, is a special business system with its own business models, structures, processes, programmes, strategies, partnerships and history. The causes for the crisis, on which the methods for their solution are largely dependent, only increase such a particularity.

### 3. BENEFITS OF THE CRISIS

Although the crisis is primarily an unfavourable state, which may be followed by the ruin of the company; some such situations may also have a positive effect, especially if the crisis was successfully solved. Good sides of the crisis could have been (ex. also Lalonde, 2008, p. 24; Meyers & Holusha, 1986, p. 28):

- confrontation with the existing reality and future possibilities by eliminating various deceits, self-deceptions, self-praise and misperceptions,
- change of the strategic direction by abandoning a commercial practice which has resulted in being unsuccessful, and the creation of new strategies and goals of the organization,
- the construction of new basic skills and the emergence of new competitive advantages based on new management models,
- management clean-up, especially the executive management, because the incompetent, unnecessary or those ready for retirement leave one way or another,
- the occurrence of new management, usually young heroes who are effectively dealing with critical situations and thus develop the best leadership skills,

- development of an early warning system and an increase in security and flexibility,
- the acquisition of new knowledge and experience from the most demanding business problems (learning from the crisis),
- the crisis acts as an initiator of changes and the reconstruction of the organizations, which were impossible before due to the high resistance to changes,
- the opportunity to change the braking and “poisoned”, into a healed (re-inspired) culture, in which the individual goals and objectives of the company are consistent,
- adjustment of the number and composition of the staff to the necessary productive jobs,
- the resolution of standing, long-lasting and ineffective civil cases and conflicts, which are enabled only by emergency situations and changes.

On the other hand, a crisis also brings some advantages, but mostly opens up new opportunities which would not have been possible in a different situation. With regard to this, some authors (Fink, 1986, p. 15; Lalonde, 2008, p. 24) draw attention to the double meaning of the crisis, which can be best expressed in the Chinese language, where the crisis is composed of two words wai-qui (or wei-chi), whereby the first part of the word means danger and the other opportunity. Therefore, the crisis “is not always the tragic fate of the company, but also the greatest opportunity for its reconstruction.” When determined balances, which characterize the normal state, get destroyed, an emergency situation occurs, which may have the character of development opportunities or a crisis.

The biggest “wealth” of the crisis, which however cannot be achieved merely by its simulation, is the acquisition of new knowledge, which the company would otherwise find it impossible to obtain. Crises always require innovative, radical and courageous ways of management or the acceptance of the most difficult business decisions, and finding a way out of the most complex situations, which are characterized by the particularities mentioned above. In such cases, the routine (routine = behaviour derived from habit) gives way to intuitive, inventive, unique and specific decisions, which require new or additional knowledge and skills. Functioning in the most difficult moments also brings the most opportunities for learning (also with the help of so-called shock therapy).

Sometimes it becomes evident that the quality of decision-making in crisis situations, where there is no time for lengthy negotiations, delays and finding a common denominator, which is characteristic of bureaucratic organizations, is even much higher. However, learning from the crisis does not come by itself, thus it will be necessary to properly organize and execute systematically the process of obtaining such knowledge. Elliot and Smith (2007, pp. 276–278) list several obstacles in learning from a crisis, which should be eliminated within the scope of a comprehensive reconstruction of the company: the rigidity of the fundamental convictions, values and attitudes; inefficient communication and information problems; ignoring external views; various (self-)deception; cognitive small-mindedness; poor flexibility; lack of corporate liability; focusing only on occasional trainings.

It is not uncommon for a company to return to the old path of inefficiencies after the successful battle with moments of crisis, however, it had not been taken up by any positive behaviour, which is referred to as the “amnesia syndrome” (Boin & Lagadec, 2000; see also Lalonde, 2008, p. 219; Roux-Dufort, 2000, p. 54). Namely after the first encouraging signals, the internal participants often reduce their efforts and concentration, and thus there is no desired phase of learning from the wasted experience gained from the worst periods of operation.

Therefore the crisis has to be the initiator and director of the renewal of the company. In order to achieve the renewal (reconstruction, transformation) of the company, it is often a condition to firstly solve this acute crisis, which could cause not only the decline of the company, but also its ruin. The successful reconstruction of a company is often the result of a preliminary serious crisis, since the reconstruction of business processes and structures, which enable the effective and efficient operations, would not have occurred if the company had not been forced to change the (less successful) business models, methods and strategic directions. The crisis should therefore be seen as a dynamic process of legitimation, de-legitimation and re-legitimation (’t Hart, 2008, p. 89). Crisis as a catharsis (= multi-layered clean-up) calls into question the past, present and possibly future actions (Simon, 2009, p. 187). In several surveys it is stated that 7 out of 10 companies are trying to create innovative business models, and 98% are modifying existing ones (Casadesus-Masanell & Ricart, 2011) and majority (54%) of more than 4,000 senior managers from the Economist Intelligence Unit favoured new business models over new products and services as a source of future competitive advantage (Amit & Zott, 2012).

In the event that the crisis is followed by the collapse of the company, of course there are much fewer benefits, and we can narrow them down to:

- the termination of the possible long-term agony of the company (long-term insolvency, increase in resource constraints, mounting debts and the reduction in the value of assets, lack of resources), which brings no benefits to anybody;
- take-over of fixed tangible and intangible assets (e.g. brand, distribution network) or production-sales programmes, which could have been useful to other companies or the broader social environment (new jobs, asset reuse etc.) and brought more added value;
- formation of “phoenix companies”, emerged from the collapsed company by taking over the healthy cores without having the burden of the possibility of an efficient and successful operation;
- faster, although as a rule the reduced payment of creditors from the bankruptcy or liquidation estate;
- the exercise of employees' rights in the event of job losses due to bankruptcy or liquidation (the allowance);
- final settlement of the specified proportions, which was not possible at an earlier stage (even the resolution of protracted disputes or personal conflicts etc.);
- clarification of unclear or hidden past events and the enforcement of responsibilities.

#### 4. EMPIRICAL EVIDENCE

In the previous discussion it had been highlighted that the crisis – which creates a distressing, uncertain and worrisome situation, which endangers property as well as people and influences established business and life flows – may also bring numerous positive effects or benefits in many areas. Therefore, we selected a sample of companies in the acute crisis and we wanted to find out whether such companies really take advantage of the crisis to improve operations by introducing the “good side” or benefits of the crisis. Since with the approach subsequently set forth, it was not possible to deduce all the aspects, we focused mostly on changing the business model (a system of interconnected and interdependent activities that determines the way the company “does business” with its customers, partners and vendors, Amit & Zott, 2012), which would turn currently inefficient business practices into a successful operation and grant the company its further survival and development (cf. Amit & Zott, 2012; Casadesus-Masanell & Ricart, 2011; Hienerth, Keinz & Lettl, 2011) in order to transform as a phoenix from an acute crisis to a promising company.

To determine whether these findings are indeed correct, the author researched measures, which were planned or implemented by the companies in an acute crisis in Slovenia during 2008-mid 2013 and attempted to solve the crisis with an insolvency procedure of a compulsory arrangement (in-court restructuring, debtor in possession proceedings), started on their proposal by the authorized court (the list available at [www.ajpes.si/eobjave](http://www.ajpes.si/eobjave)). If bankruptcy is a method of solving an out of control crisis, then a compulsory arrangement is a method of recovery, where the creditors play the key role. The creditors will not accept the proposal of a distress company, worsening the status of their claims if they cannot see radical changes in business practice of the debtor. Therefore, it would be expected that new strategies, structures, processes and systems are presented in the distress company in the frame of the new business model that should replace previous ineffective business practices that led to the acute crisis. As mentioned earlier crisis recovery cannot be successful if it is not applied simultaneously in business (substantive) and financial areas (e.g. Kraus & Gless, 2004, p. 121; Seefelder, 2007, p. 27). Only from financial restructuring a distress company cannot ensure its further existence and development.

A well prepared and executed compulsory arrangement is often a necessary, yet insufficient condition for achieving a drastic change and ensuring re-development in a company. An insolvency procedure is a process, not a solution (Miller, 2008, p. 202), which gives a company time and access to new ways of financing for the recovery and renewal. A compulsory arrangement is thus only one of the steps in saving a company, which, however, does not ensure its successful future business, but is vital for the implementation of further steps to solve the crisis (threat of bankruptcy).

Out of 163 studied cases of companies in compulsory arrangement only 14 (8.6%) included in their key recovery measures the introduction of the new business model which should represent a healthy fundament for further successfulness and as many as 91.4% of companies focused only on the



various forms of financial restructuring (without any serious changes in business orientation and operations). This research, other previously mentioned empirical researches and author's own many years' strategic management and restructuring consultancy practice have shown that such companies:

- in most cases attempt to solve the acute crisis with various forms of financial restructuring, meaning that they are actually dealing with the consequences rather than the causes of the crisis, which have brought on the need for financial disburdening;
- approach crisis problems with short-term financial methods, burdening their creditors and causing a crisis chain reaction reaching their suppliers;
- pay surprisingly little attention to the changes of their ineffective business models (that led to the acute crisis) and introducing new strategies, structures, processes and systems, even though in this case this is the most important area of renewal, which will ensure further existence and development;
- will apparently even after financial disburdening continue to burden their creditors by continuing to rely on existing unsuccessful business models, thereby exposing the company to another imminent acute crisis;
- are mainly only dealing with short-term and superficial measures, although the extent of the crisis is very deep and encroaching upon several areas (Table 1), among the prepared measures there is particularly exposed the legal aspect (which is expected with regard of the type of the sample) and financial perspective, as part of the broader economic perspective; meanwhile unexpectedly little attention is paid to other aspects, especially the traditional – as a break with previous practice and start a new business life cycle of the organization, the formation of new foundations to build the core capabilities of the organization and competitiveness factors, and the introduction of a new managerial ideology and approaches – which in this case were studied with a radical change or the introduction of new business models.

Research of the adopted measures of companies, which are attempting to solve the crisis with an insolvency procedure of a compulsory arrangement (in Slovenia in the period 2008–mid 2013), has shown that the survival rate of these companies in the next five years will be extremely low (perhaps 15–20%), since they are addressing the resolution of the crisis in the short-term, superficially and limited only to certain aspects, although the acute crisis in its definition has unprecedented proportions (Table 1), meanwhile the “good side” or the benefits of the crisis remain untapped, and these do not come by themselves. One of the key reasons is neglecting the need for a complete change of the existing business models, despite the fact that “there has never been as much interest in business models as there is today” (Casadesus-Masanell & Ricart, 2011), where it would be necessary to focus on the causes of the acute crisis (more difficult), whereas companies tend to focus more on the consequences of their crisis and the measures of short-term financial disburdening (simpler), which provides no guarantee to the participants that the crisis in these companies will actually be solved even for a mid-term time period.

We recognize the limitations of the research and that the financial restructuring plans, from which were obtained the information, as the central documents in the composition proceedings which are replacing the rehabilitation programme, are not necessarily the actual strategic business plans, since the primary purpose of the financial restructuring plan is to convince the creditors to a positive vote in the proposed settlement (review optimistic outcomes), and therefore may not include all the measures envisaged, however, the creditors will decide on the financial write-off for the insolvent company on the basis of these substantive measures.

The findings of the research presented here are otherwise consistent with the author's previous researches. In the study in 2009, there was selected a sample of surveyed firms (107) from the list of employers with which the Employment Service of Slovenia concluded an agreement on the partial subsidization of working time (as of April 2009), which is based on the partial subsidization of full-time employment, which was adopted by the Government of the Republic of Slovenia in order to mitigate the financial and economic crisis, however, it has been shown that 90.6% of respondents considered that the measure of the partial subsidization of working time by the state was not sufficient for the problems to disappear, meanwhile only a quarter (23.5%) said that this was part of their broader rehabilitation programme (others believed that this is due to a temporary decline in orders and the scope of work, and take no other measures). The sample encompassed companies (with 10 employees or more) which were in difficulties in one way or another, and have consequently applied for the state subsidy. Although the companies were aware that obtaining a grant is not sufficient, as

much as three quarters of these companies had not prepared any other actions within the scope of a wider rehabilitation programme (Dubrovski, 2011, p. 179).

## 5. CONCLUSIONS

Based on several empirical researches, author's own strategic management and restructuring consultancy practice in 80 companies from various branches in Slovenia from 1994-2013, working also as crisis management and insolvency practitioner, including the research described in this paper it can be *clare et distincte* stated that replacing the current ineffective business models with new business practice is an essential part of recovery of a company from crisis and ensures its further survival or accelerated development.

The study of 163 Slovenian companies which attempted to solve the acute crisis during 2008 – mid 2013 with an insolvency procedure of a compulsory arrangement, has unfortunately shown that in these cases the reorganization programme was primarily based on short-term financial restructuring and not a overall business renewal, which would require an initial marketing restructuring, followed by technological, development, production, human resources and other areas of restructuring, acting as a key factor in the future existence and development for at least a mid-term period.

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