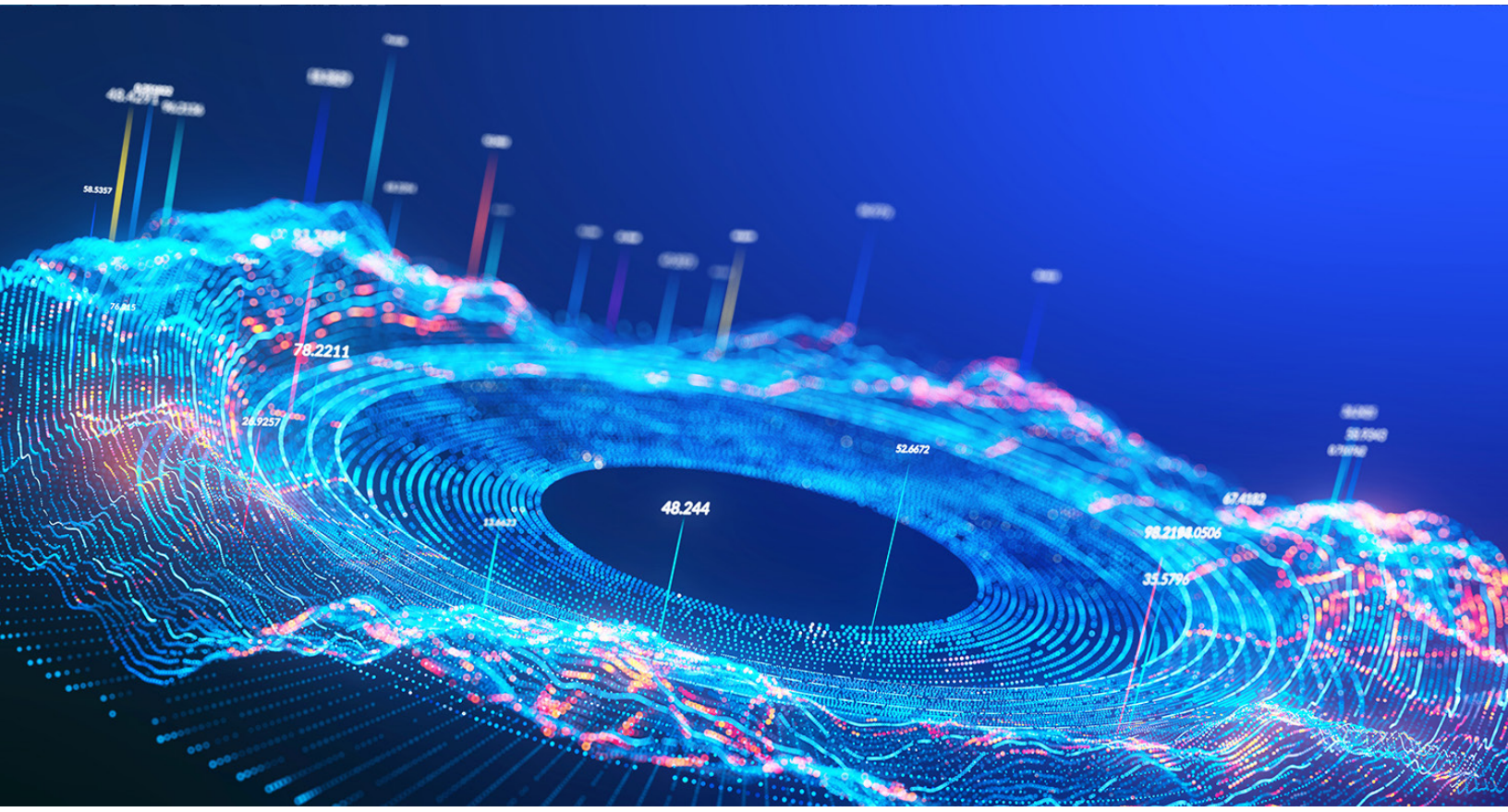
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Industrials Practice

Regaining the competitiveness of Europe's industrials the European way

Our research shows that 45 percent European industrial companies exhibit heightened levels of financial stress or even distress. Six proven turnaround approaches show how companies can respond.

This article is a collaborative effort by Philipp Espel, Andreas Tschiesner, José Pimenta da Gama, Sébastien Lacroix, and Tunde Olanrewaju, representing views from McKinsey's Strategy & Corporate Finance and Industrials Practices and McKinsey Transformation.



November 2026

Anyone who follows European industrials knows the typical headlines: A chemicals conglomerate issues its third profit warning in 18 months. An automotive supplier grapples with falling orders and overcapacity. A components maker idles a plant as energy prices bite. Each adds to a well-worn story of challenges and decline in the sector.

However, for a few such players, we have seen this picture change in a matter of months: The same chemicals conglomerate went on to create positive free cash flow of more than €1 billion. The automotive supplier tripled its EBITDA. The components maker doubled its share price. Each company faced its challenges and successfully managed an at-scale performance transformation under European conditions that bucks this narrative.

These examples matter because of what is at stake. Industrial companies in Europe are a backbone of the region's economy, accounting for about 36 percent of value added, 29 percent of jobs, and more than 45 percent of R&D.[1] Yet this industrial engine is struggling to maintain its competitive position against other countries, particularly China.

An index of financial health we compiled shows that almost half of European industrial companies are showing signs of financial stress or distress. Nevertheless, their problems are structurally fixable. They are better positioned to overcome these challenges than the broader headlines suggest.

In this article, we draw lessons from years of helping clients restructure and from several recent at-scale transformations to identify six turnaround fundamentals that have proved successful in European conditions; these are repeatable across companies and sectors.

Europe's industrial inflection point

The issue of Europe's waning competitiveness and how to reverse its decline has been the subject of numerous recent reports—including, notably, from Mario Draghi,[2] the former president of the European Central Bank, in 2024, as well as research from McKinsey.[3] For industry specifically, higher costs for labor and energy have eroded Europe's past advantages (Exhibit 1).

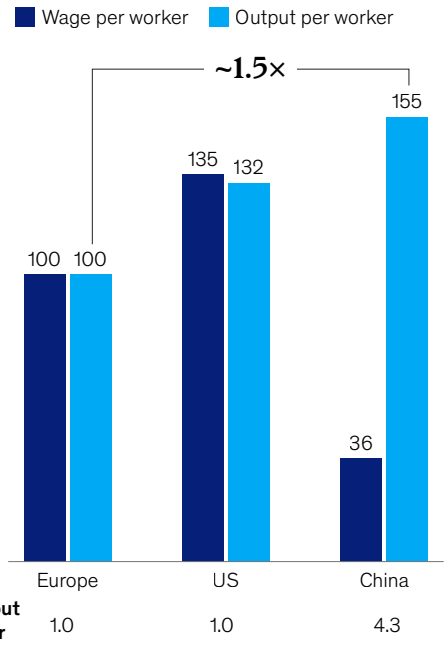
An index of financial health we compiled shows that almost half of European industrial companies are showing signs of financial stress or distress.

[1] Data from Eurostat and the 2025 EU Industrial R&D Investment Scoreboard.
[2] Mario Draghi, *The Draghi report: A competitiveness strategy for Europe*, European Commission, September 9, 2024.
[3] "Accelerating Europe: Competitiveness for a new era," McKinsey Global Institute, January 16, 2024.

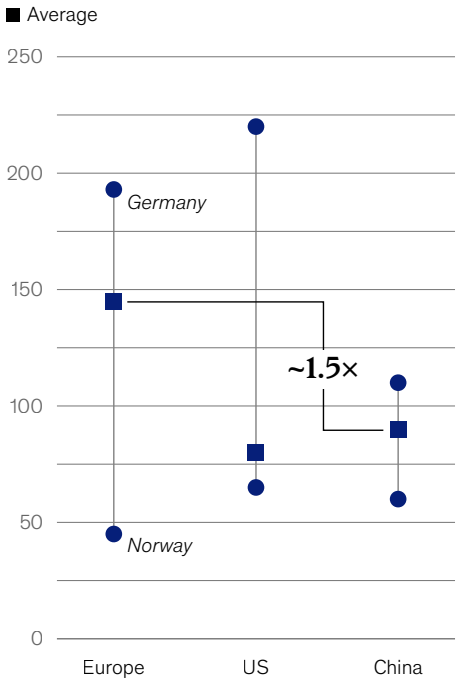
Exhibit 1

European industrial companies face disadvantages in main cost driver categories.

Automotive R&D for state-of-the-art plant, example, indexed (EU = 100)[1]



Electric power prices,[2] $ per megawatt-hour



[1]Productivity is measured by unit output per full-time equivalent (FTE): % of platform output per FTE for a R&D electric vehicle platform.
[2]Industrial electricity prices, indicative $/MWh, 2024 and 2025; including grid costs and taxes and excluding subsidies.
Source: Bloomberg; China National Development and Reform Commission; CME Group; Eurostat; Korea Electric Power Corporation; Nord Pool; S&P Global Market Intelligence; UK Department for Energy Security and Net Zero; UK Office for National Statistics; US Energy Information Administration; World Bank; McKinsey Global Institute analysis; McKinsey POBOS

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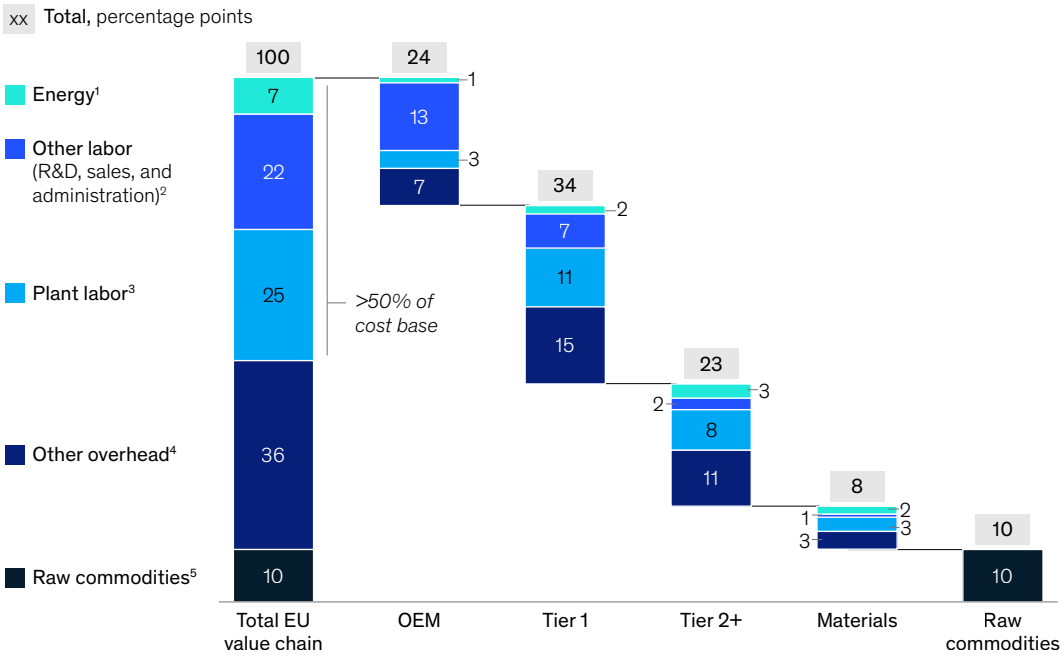
On labor productivity, EU and US wages are higher than in China, while output per full-time equivalent is now lower, according to McKinsey analysis. As a result, labor productivity for Chinese industrial output is 1.5 times higher than that of Europe. Energy costs also are higher in Europe—on average more than 1.5 times costs in China and the United States.

We quantified the impact of these disadvantageous factors on the profitability of European industrials. For the total industrial EU value chain, we found that more than 50 percent of the combined cost base is adversely affected (Exhibit 2). Approximately 47 percent of the integrated value-chain costs are labor-related, and approximately 7 percent are exposed to energy price differences. Put differently, for half of average European industrial profit and loss (P&L), European incumbents are already behind by a factor of 1.5 times or more.

Exhibit 2

Across the value chain, more than 50 percent of the cost base is at a disadvantage to China from labor and energy cost levels.

Industrial and automotive cost base in Europe, German plant example, % of today's cost



Note: Figures may not sum to totals, because of rounding.
[1]Electricity, gas, and process heat purchased. [2]Personnel outside the plants in engineering, sales, and administration (~66% of R&D and SG&A). [3]Direct and indirect plant personnel, incl maintenance, logistics, and quality. [4]Depreciation, scrap, nonpersonnel maintenance, logistics, R&D, SG&A, and warranty. [5]Material input of tier 3 at world market prices.

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As a result, a spiral of deterioration is developing (Exhibit 3): Lower productivity leads to worse piece-cost economics, which leads to lower returns, which leads to higher financing costs and, thus, lower investments. This is already visible today. Europe is losing investment share against China and the United States. Gross productive investment, a proxy for current competitiveness, has soared in China over the past three decades, reaching an annual total of about $6 trillion in 2025. By contrast, investment in Europe has remained relatively flat, at around $3 trillion in 2025.[4]

Almost half of Europe's industrial companies show heightened levels of financial stress or distress

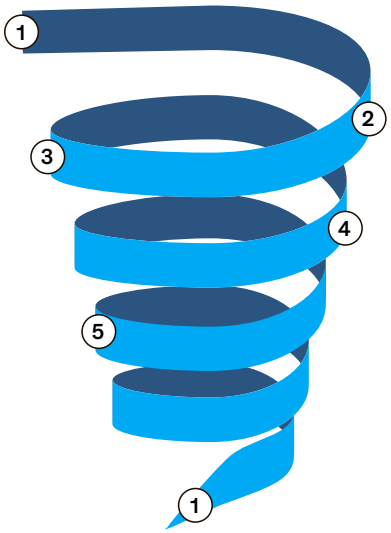
To gauge the full effect of these structural pressures, we compiled a proprietary McKinsey Industrial Financial Health Index that scores Europe's industrial companies as either healthy, stressed, or distressed (see sidebar, "About McKinsey's Industrial Financial Health Index"). In all, the index includes almost 1,200 public and private companies, each with revenue of more than €100 million.

[4] "Catalyzing competitiveness: Where investment happens and why," McKinsey Global Institute, June 30, 2026.

Exhibit 3

Many European industrial companies are facing a cycle of decreasing competitiveness.

Factors contributing to lower levels of competitiveness



1. Lower competitiveness	• Core productivity indicators below benchmark • Unit costs in calculations too high • Cost plus model leading to noncompetitive prices
2. Cash return decreases or cash breakeven increases	• Low or negative cash return per unit sold • Not enough cash to cover indirect and overhead cash-out
3. Lower internal financing power, interest rate burden	• Low or negative cashflow from operations • Headroom to covenants decreases • Increasing cost of external financing
4. Lower investment, less innovation	• Investment for innovation (after replacements) decreases • Emergency cuts of R&D projects • Sell-offs of growing or future portfolio elements
5. Volume drop, lower unit margins	• Fewer new-business acquisitions • Lower ability to compensate annual customer continuous improvement process claims • Quality or delivery issues due to lack of maintenance, savings in quality cost, etc • Loss of fixed-cost absorption → Lower competitiveness

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About McKinsey's Industrial Financial Health Index

McKinsey's Industrial Financial Health Index converts five financial signals into a single score per company per year. Based on the score, companies are classified into one of three buckets: healthy, stressed, or distressed.

The five financial signals were chosen to cover a current perspective on a company's profit and cash situation (year-on-year EBITDA change, cash cycle days change, and EBITDA to interest) as well as a forward-looking perspective (net debt to EBITDA and the percentage of total debt maturing in the next two years).
For each signal, we defined a threshold that, if breached, results in a certain score being added to the total. Four indicators each carry a flat 0.5 points if breached: an EBITDA decline of 20 percent or more year over year; cash cycle lengthening by 15 percent or more; EBITDA-to-interest coverage at or below 1.25 times; and 25 percent or more of debt maturing within two years. Breaching all four adds up to 2.0 points.

Leverage (net debt to EBITDA) is scored separately on a sliding scale: Between 2.0 and 3.0 times scores 1.5, and more than 3.0 times scores 2.0. Combined with the four flat indicators, the maximum score is 4.0. The higher weight for leverage stems from its importance as a covenant in many external financing setups.

Companies scoring 1.5 are deemed stressed, those scoring 2.0 or higher are deemed distressed, and all other companies are classified as healthy.

The Financial Health Index is calculated based on available full-year 2025 data from S&P Capital IQ for all industrial companies—that is, those active in manufacturing goods—in Europe. Our definition of industrials includes companies in process and materials; electrical and electronics; and machinery, automotive, and assembly.

The index shows that about 45 percent of the companies registered as either financially stressed or distressed in 2025. That was three percentage points higher than in 2024 and six points higher than in 2023. Preliminary data from 2026 suggest that the slide is accelerating. That puts about 3.7 million jobs and more than €500 billion in value add directly at risk. And no country is immune. For example, Portugal, Luxembourg, the Netherlands, and Spain show a very high share of industrial companies in financial stress or distress, and Germany's share increased by 12 percentage points (Exhibit 4).

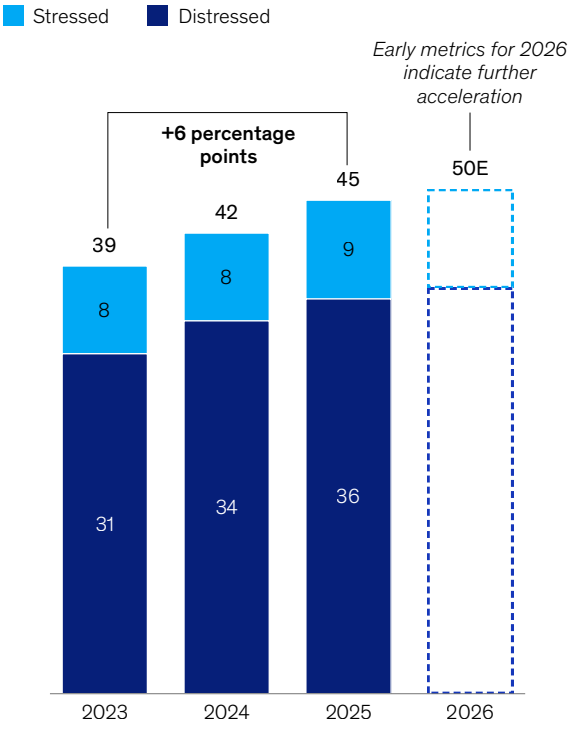
Success case studies: Industrial restructuring that works

Decline is not inevitable. Indeed, there is considerable opportunity for an industrial comeback that could lift the fortunes of European companies through in-depth transformation. To that end, we investigated five recent European case studies that successfully countered these challenges: an automotive and technical supplier, a chemicals producer, an automotive supplier, a components maker, and an industrial components manufacturer. Outcomes of the transformations in these cases included a swing to more than €1 billion in free cash flow, tripled EBITDA, and a 100 percent gain in share price. While these situations had different starting points, they all lead to the same conclusion: At-scale performance transformation is achievable in Europe's constrained environment.

Exhibit 4

The share of Europe's industrial companies in financial stress or distress has rapidly increased since 2023.

European industrial companies, economic status by Financial Health Index, 2023–26, %



Countries ranked by 2025 share of industrial companies in financial stress or distress[1]

High share Medium share

		2024	2025	
1	Portugal	High	High	Strong increase
2	Luxembourg	High	High	Strong increase
3	Netherlands	High	High	Increase
4	Spain	High	High	Increase
5	Norway	Medium	High	Strong increase
6	Italy	High	High	Increase
7	Finland	High	High	Decrease
8	United Kingdom	High	Medium	Decrease
9	Ireland	Medium	Medium	Increase
10	Poland	High	Medium	Decrease
11	Denmark	Medium	Medium	Strong increase
12	Germany	Medium	Medium	Strong increase
13	Austria	High	Medium	Decrease
14	Sweden	Medium	Medium	Increase
15	Belgium	Medium	Medium	Increase
16	Switzerland	Medium	Medium	Decrease
17	France	Medium	Medium	Increase

[1]Showing top 17 countries only.

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A key takeaway from these and other transformations is that there is no single fix. Rather, a balanced set of actions need to be taken in parallel, as outlined below. Across the case set, for example, the impact split roughly among various balance sheet and P&L items: Improved commercial measures accounted for about 20 to 50 percent of the impact, material costs 15 to 35 percent, manufacturing and operations 15 to 55 percent, cash (including both capital expenditures and net working capital) 5 to 25 percent, engineering and R&D 3 to 10 percent, and reduced general and administrative expenses 2 to 5 percent. The impact per P&L function varied depending on each company's starting point, but the rerating consistently came from moving across all of them at once.

Beyond the question of which P&L and balance sheet items were addressed, the cases converged on how the transformation was run. Six recurring success factors explain the difference between programs that deliver and those that stall (Exhibit 5).

Exhibit 5

Successful turnarounds are often built on six success factors.

Insights from European industrial turnarounds

Governance and steering

1. Organizing for success
Recognize that the structure that created the issues won't fix it

Make conscious trade-offs to move away from business as usual:
- Organize around a task force to cut across line accountability.
- Accelerate cadence and drive decisions top-down.
- Steer ex ante with a system of improvement action control.
- Establish a dedicated role carrying overall performance accountability.

6. Keeping administrative burden light by leveraging AI
Use AI for a step change in velocity and steering

- Successful turnaround programs achieve broad engagement and allow real-time issue identification. For this, five elements remain essential: Transparency, granularity, sized financial impact per measure, reconciliation with profit and loss, and senior leadership attention.
- Putting these elements in place comes with an administrative burden that can be reduced by 40% when leveraging AI.

Operational

2. Raising labor productivity
Go through the works council for the fastest route to productivity

- Addressing 12 labor productivity levers can cut conversion costs by 7–18%, adding about 7 percentage points (p.p.) to total margins.
- Higher labor productivity can take two routes to higher competitiveness:
  1. Increase volumes, innovate, and achieve lower cost point.
  2. Reduce work volume measured in costs.

4. Addressing wasteful spending
Optimize your spending for a clean sheet and a new reality

- Typically, >20% of nonproduction spend, capital expenditures, and net working capital can be reduced without harming core value creation.
- Challenge boards are used to control investment behavior, and optimizing engineering specs reduces costs by 15–20%.
- Granular management of entire spend cube allows for significant short-term cost savings.

3. Growing in markets that aren't growing
Avoid leakage and unlock segments and adjacencies

20–50% of impact came from commercial levers in the cases we investigated:
- Protect the core: Drive tight margin protection in contract execution, yielding +1–2 p.p. EBITDA.
- Grow the core: Move from "gatherer" to "hunter" as 20% of revenue is expected to go to new players.
- Unlock adjacencies.

Structural or portfolio

5. Consolidating portfolios to free up underperforming assets
Revisit the portfolio in a granular and bold way

- Prune the portfolio systematically and make decisions on a net-present-value basis to fix, close, or sell.
- Divesting units to their "best" owner could create up to €60 billion in value.

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A key takeaway from winning transformations is that there is no single fix and no silver bullet that works for all. Rather, a balanced set of actions need to be taken in parallel.

1. Organizing for success

About 70 percent of transformations miss targets, and about 55 percent of the value is lost in implementation and after the program, according to prior McKinsey research.[5] Successful turnarounds deliberately break with the company's standard operating model along four dimensions, and each is a conscious departure from business as usual.

First, they organize around a task force instead of the line organization. A turnaround has to break with the current way of working; the line organization, the very structure that produced the underperformance, cannot be relied on to reform itself. Leadership therefore installs a temporary transformation governance layer that deliberately overlays the accountability of line owners. This temporary layer has a license to shake up the status quo and enforce fresh thinking. At a later stage, once new behaviors take hold, this task force is absorbed back into the line organization, which will usually look different after the turnaround as the new operating model becomes the permanent way of working.

Second, successful turnarounds make decisions top-down and at an accelerated pace. Decision cadence accordingly compresses from the business-as-usual monthly or quarterly rhythm to a rhythm measured in weeks.

Third, successful turnarounds control improvement actions proactively rather than simply tracking financials afterwards. Financial impact is a result that materializes late in the year. Numbers reported early in the year represent only a promise or commitment and are not yet grounded in physical change. Successful turnarounds therefore establish a system for controlling improvement actions that reveals early on whether sufficient potential is actually being addressed, typically using an action-tracking tool, ramp-up curves, and funnel management from idea to run-rate value. This shifts the conversation from explaining past results to steering future ones.

Last, successful turnarounds establish a dedicated role to carry accountability for overall business performance instead of leaving that accountability distributed across line managers responsible only for their own areas. A chief transformation officer mandated by the CEO and shareholders roughly doubles success rates, according to McKinsey research. A strong person in this position can deliver up to 25 percentage points more impact after 1.5 years, and they can implement a greater volume of measures on time (up to 15 percentage points more).

[5] "Losing from day one: Why even successful transformations fall short," McKinsey, December 7, 2021.

2. Raising labor productivity

As discussed above, regaining competitiveness for European industrials implies revamping labor productivity in Europe. Based on our sample case studies and our extensive work in operations, we identified 19 cost levers in industrials, 12 of which are labor-related. These range from enhancing shop-floor productivity, improving overall equipment effectiveness, implementing smart automation in direct work, to simplifying and automating indirect work, increasingly using AI (Exhibit 6). Measures can also include reducing ineffective management layers and standardizing portfolios.

Quantifying the impact of these levers across the value chain shows a significant improvement is possible: If all levers were applied simultaneously, total labor cost reduction worth 7.4 to 17.7 percent of conversion cost could be achieved, depending on the tier of the value chain. Applied to the industrial end product and combined with other levers, this could equal a profitability improvement of 7.3 percentage points. (For comparison, the average profit margin of industrials in Europe is around 4 to 6 percent.)

Translating better labor productivity into better competitiveness can take two routes. First, companies can use the higher output to sell more product, work on innovation, and achieve better cost positions, among other benefits. In other words, they can collaborate with the labor force to provide additional capacity for more revenue and profit generation. This requires growing markets (or capturing market share). That is challenging for European industrials at a time when global growth rates, and especially European home market growth rates, are muted. Current forecasts project negative growth for manufacturing output with only a modest rebound expected during the next several years.[6] The second route is to reduce the work volume as measured in cost—that is, the number of hours times the cost per hour companies deploy.

The European system offers a viable HR toolbox for structural workforce transformation measures covering three types of intervention. The first is reducing the cost per employee through changes to overall salary or benefits costs. The second is increasing working time per employee (maintaining the same salary) through adoption of working hours practices. For example, in Germany, there is an ongoing debate about increasing core weekly hours, moving from daily to weekly limits for more flexible production shift schedules, and increasing total annual hours worked such as through incentives. The third is reducing overall headcount cost through hiring freezes, natural attrition, and last-resort separation agreements. Together, these measures can reduce labor costs to higher productivity levels.

While labor-related issues are highly regulated in many European countries, legislation on codetermination provides some degrees of flexibility and viable European-specific routes to achieve labor productivity moves through negotiated agreements, often with employment guarantees, investment, and operational commitments on the employer side.

Our success cases also illustrate what is possible if labor cost is addressed in a stringent and targeted way: Three companies reduced labor costs by more than 15 percent. The reduction materialized during a 12- to 18-month period without larger disruptions such as protests or strikes. This was possible because of the involvement of codetermined supervisory boards; the use of natural attrition (the natural movement of employees through retirement, job changes, and other circumstances) and transfer platforms; a professionally managed transfer matrix process; communication from top management; and collaborative negotiations with labor representatives.

[6] For example, see "Autumn 2025 Economic Forecast shows continued growth despite challenging environment," European Commission, November 17, 2025; or *Economic and steel market outlook 2025-2026: Q4 report,* EUROFER, December 2025.

Exhibit 6

Labor productivity levers can cut conversion costs by 7 to 18 percent, adding about seven percentage points of margin across the value chain.

Operational performance improvement levers

Labor levers

Cost block	Lever (what the plant does)	Improvement rate, %	Effect on conversion costs, % (Low → High): Tier 0 or OEM	Tier 1	Tier 2+	Materials
Direct labor	Design-to-manufacturing and work content	10	5.8	2.7	2.2	1.0
	Uptime optimization and scheduling	5	2.9	1.4	1.1	1.0
	Inline quality or first-time-right	3	1.7	0.2	0.3	0.1
	Absenteeism reduction	3	1.7	0.8	0.7	0.6
	Automation of manual process step	5	2.9	1.4	0.8	0.3
	Variant and portfolio simplification	2	1.2	0.5	0.3	0.1
Indirect blue-collar labor	Lean logistics and quality organization	5	0.2	0.6	0.5	0.5
	Automation of logistics and inspection	5	0.2	0.6	0.3	0.2
	Capacity consolidation and utilization	5	0.2	0.6	0.5	0.5
Indirect white-collar labor	Process simplification of indirect work	10	0.3	1.6	1.0	1.2
	Automation of indirect work (gen AI)	10	0.3	1.6	1.0	1.2
	Span of control and management layers	5	0.2	0.8	0.5	0.6
Labor levers subtotal, % of conversion cost			17.7	12.8	9.2	7.4
Energy	Energy management (load, shutdown, and recovery)	8	0.6	0.6	1.2	1.8
	Energy-efficient equipment	5	0.4	0.4	0.8	1.2
Other overhead variable	Maintenance strategy for material and services	10	0	0.6	0.9	0.9
	Consumables and tooling management	10	0.2	0.3	0.9	0.4
Scrap	Process stability and inline quality control	20	0.2	0.6	1.0	0.4
Other fixed overhead	Smart automation of maintenance	10	0.4	0.6	0.3	0.3
	Footprint consolidation	10	0.1	0.6	0.2	0.2
All levers total, % of conversion cost			19.7	16.5	14.5	12.5
Adjusted total, correcting for overlapping effects, % of conversion cost[1]			**17.9**	**15.3**	**13.7**	**12.0**

Considering share of conversion costs in total product costs for each tier, **the total effect on the entire supply chain is about 7 p.p.**

Note: Figures may not sum to totals, because of rounding. Base addressed = cost block share × share of the block addressed by the lever × plant conversion cost in % of total cost. Total cost = net revenue – EBIT. German plant's part of each step = share of the step's value added located in Germany (100%, 50%, 40%, or 20%).

[1]Calculation: all levers chained (% of conversion cost) × plant conversion cost (% of archetype's product cost) = effect (% of archetype's product cost) × product cost of the step in the vehicle value chain (percentage points [p.p.] of vehicle cost) = effect (p.p. of vehicle cost – whole chain).

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Pursuing growth in restructuring environments means steering the sales force with greater granularity and transparency.

3. Growing in markets that aren't growing

While market growth is muted, the critical steps are both protecting and growing the core as well as unlocking adjacencies. Pursuing growth in restructuring environments means steering the sales force with greater granularity and transparency.

Protect the core. In our experience, best-in-class claims and contract management can lead to an EBITDA improvement of one to two percentage points. AI-supported analytics can evaluate contracts and potentially recover profitability leakage across missing amortization to unrealized productivity due to volume reductions and fixed-cost increases. It can also help to identify business leverage in negotiations, such as single-source situations. Finally, a rigorous approach to renegotiating terms needs to characterize the execution phase: defining clear walk-away positions, cadence of escalating negotiation levers, and negotiation dry runs.

Grow the core. Developing a systematic growth engine for profitable new business is key in contracting and highly contested markets—in other words, moving from "gatherer" to "hunter" to maintain and increase market share. One example of the importance of this strategy comes from automotive, in which about 20 percent of light-vehicle revenue is expected to go to new players rather than incumbents by 2030.[7] Growing the core means defining and prioritizing the total market by OEM, products, and region and defining the list of must-win opportunities. A clear acquisition strategy is required for each opportunity, considering competitive positioning and differentiation, including technical compatibility, key buying factors, and portfolio composition. This approach can lead to a winning strategy for priority projects and can allow organizations to identify relevant stakeholders that need to be addressed, implement a market-backed pricing and negotiation approach, and establish a rigorous sales drumbeat.

Unlock adjacencies. There's often a gap between top-line aspirations and core market growth; in the case of German auto suppliers, for example, the ambition is about 4 to 6 percent growth until 2030, while light-vehicle market growth is currently only about 1 percent. We have developed a six-step approach to identify and prioritize growth opportunities and turn today's capability moats into new profit pools. This approach entails a detailed evaluation of market potential and market growth (in other words, where to play); capabilities (how to play); competitiveness (how to win); capital allocation; the business case, including investment need; and the go or no-go criteria. Together, these steps help define a mid- and long-term growth strategy.

[7] Mobility Global data.

4. Addressing wasteful spending

European industrial budgets for nonproduction spending and capital investment are usually extrapolated from previous years' levels. Increments are often scrutinized, but the base spend levels may have been unchallenged for years. At the same time, net working capital (consisting of accounts receivable, accounts payable, and inventories) is often managed toward the end of a period rather than throughout the entire year.

In our experience, fixing such issues can have substantial impact. Based on our sample, there typically is 20 percent or more in wasteful spending, investment, and net working capital levels in annual budgets that can be reduced without harmful impact to core value creation. In our experience, some approaches are particularly effective.

Capital expenditures. "Challenge boards" consisting of the transformation team and operations leaders test every planned investment on a line-item level for effectiveness. Are these items critical or not? For what reason? Could the items be postponed or reused? Are cheaper options available? These sessions conclude with a detailed, written explanation of why the investment is needed, how high the risk is, and what the cost would be in a risk event. Optimizing engineering specifications for products in detail can reduce costs per product substantially—by 15 to 20 percent for some clients. AI also has a role to play here: It can be used to establish a rapid bottom-up estimate of capital expenditures based on product design and the assembly process. The aim here is not simply to spend less but to improve the effectiveness of the investment.

Spend control. AI can also be brought in to optimize accounts payable and accounts receivable, centralizing spending controls and helping fund the transformation internally, thereby reducing dependence on third-party financing. A core lever here is the granular management of the "spend cube"—that is, the extensive matrix of budget-owning organizational units (at the most granular level, ideally department level or below) and spend categories (ideally cut into 20 spend categories or more). AI agents can support four activities: finding value by identifying cash opportunity pools; prioritizing actions, including by ranking action lists and helping with negotiation strategy; triggering action, especially for customer collection and dispute management; and detecting leakage.

Net working capital. Expert input and AI can be used to develop cleansheets identifying the optimal inventory level per industrial site. This starts with clean and structured inventory data to develop supply chain assumptions that are then used to develop inventory cleansheets. This zero-based analysis sets optimal inventory levels for each site-specific context. The cleansheets help guide execution by combining operation and strategic levers, such as supplier and customer negotiations. They also flag any leakage against the target.

5. Consolidating portfolios to free up underperforming assets

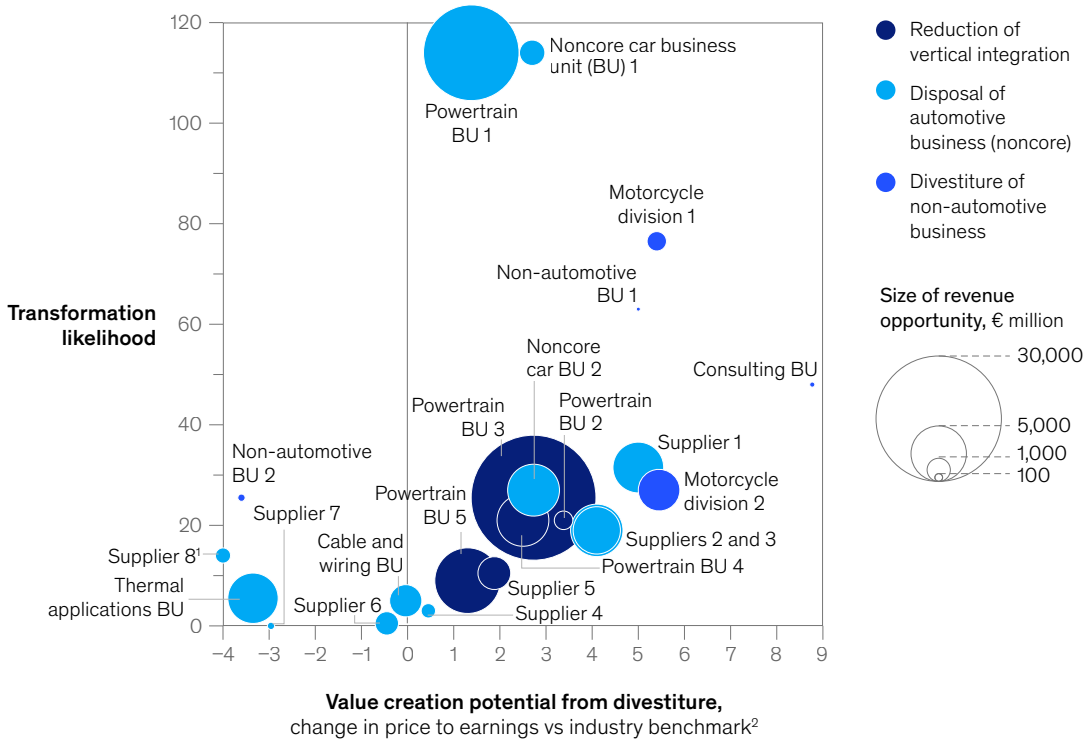
Most European industrials are companies with multiple business units that own a portfolio of different businesses, including those with different technology offerings, those that focus on different product markets, and those that pursue different business models (for example, OEM, aftersales, and adjacent services). Most portfolios grew historically, and the performance of individual units varies widely. This can lead to a situation in which substantial capital is tied up in assets that are linked to underperforming businesses.

To show the improvement opportunity hidden in this status quo, we analyzed the European automotive sector as an example and assessed how much value could be created by unfreezing the assets of underperforming businesses and combining them with a "best owner" (Exhibit 7). To size value creation potential, we first computed the delta in the current owners' price-to-earnings ratios and then compared it with the price-to-earnings ratio of the benchmark for the specific business segment. This analysis thus

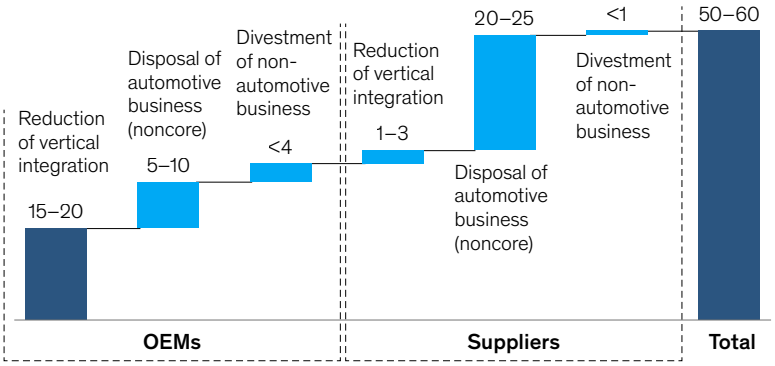
Exhibit 7

The landscape of possible portfolio moves shows up to €60 billion of potential.

Transformation likelihood, deal experience or carve-out ability[1] (with increasing likelihood, where 0 = very unlikely)



Potential deal value of portfolio moves, (outside-in[3] EU), € billion



[1]Plotted at axis minimum (adjusted price-to-earnings delta is −42).
[2]Indicated by number of deals since 2008, adding 50 points in case of easy carve-out ability and deducting 50 points in case of difficult carve-out ability. Reduced by 50 points if remoteness of business is only medium rather than high.
[3]Revenue used as 1:1 multiple for transaction.
Source: S&P Global Capital IQ; McKinsey Corporate Performance Analytics

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assesses whether the current ownership structure leads to a discount on the value of the assets. Second, we assessed the transaction complexity based on size of a deal and the ease of carving out the business.

We found that in automotive, a value increase of more than 20 percent, or up to €60 billion, is possible through such portfolio consolidation. The upside stems from, first, scale benefits—for example, because of purchasing volumes or asset utilization; second, higher and more targeted investment because of consolidation and thus more innovation; third, removal of redundancies in overhead and indirect areas; and fourth, elimination of cost incurred today to stabilize struggling (subscale, nonperforming) players in the value chain.

In our turnaround success cases, two major approaches were deployed: pruning the portfolio in an accelerated way and building alliances.

Pruning the portfolio. Stranded assets are cleaned up by fixing, selling, or closing business units, products, and plants. This requires a systematic review of the portfolio to identify assets where the company is not the best owner and where return on incremental investment is below the company's capacity or ability to fund. In our experience, structured pruning has three steps. The first step is to define the unit of analysis, such as an individual asset or a cluster of assets, product lines, or entire business lines. The second is to score the attractiveness of each unit in terms of its size, growth, and margin trajectory as well as its ability to win—in other words, factors such as the advantages of ownership, market share leadership, and strategic distance from the core business. This helps determine whether an asset suffers from an underperformance that is fixable or is a structural misfit. The third is to calculate the net present value of each path to determine whether to fix, sell, or close. This calculation requires realistic assumptions about the cost of a turnaround, the timeline, and the probability of success.

Building alliances. Individually, many world-class European companies operate within fragmented value chains, some of which have duplicative national industrial bases and disconnected supply ecosystems. This puts them at a structural disadvantage to competitors with greater scale, such as US companies with tech-scale integration and Chinese peers with an investment advantage. The path forward is not simply more investment but smarter linkages: collaborations across sectors, value chains, and borders that unlock scale, speed, and capabilities without requiring formal consolidation.

We see several types of collaboration emerging. One is convergence between automotive and defense production, with existing vehicle assembly plants being converted to produce defense equipment.

A second type takes place at the procurement phase, especially joint procurement of critical raw materials. This can take the form of collective procurement mechanisms to jointly purchase such materials. Binding regulation is needed to create the legal framework for joint purchasing, with an industry alliance identifying projects and matching investors with supply opportunities.

The third type entails clusters of competing manufacturers located in the same region pooling machinery and other noncompetitive resources. For example, this could include consolidating a supplier base of specialist subcontractors or pooling academics and their lab facilities from local universities to train specialized graduates with cross-institution learning. Likewise, engineers, project managers, technicians, and service engineers can move between firms in the cluster through transfer programs.

6. Keeping administrative burden light by leveraging AI

A successful turnaround program achieves broad engagement in the organization and allows the transformation team to identify issues—such as delays in implementation or impact or emerging risks of individual improvement actions—in real time and to react promptly. For this, a few nonnegotiables need to

be in place. Historically, these have been implemented using extensive controlling tools, detailed action tracking sheets, and highly frequent, very granular reports (such as league tables, top-action lists, and delayed-item overviews). Today, AI can provide these in a way that is much lighter and nonbureaucratic.

Five of these nonnegotiables include the following:

— *Transparency.* Real-time transparency is needed to track progress and potentially trigger escalation across business units and workstreams. How it manifests: Weekly or biweekly steering committees discuss implementation progress and derive concrete actions in case of nonperformance. AI helps to produce real-time transparency from vast data, flag patterns or concerning data, follow-up autonomously, and suggest mitigation measures.

— *Granularity.* Detailed measures need to have an attributable impact and only one owner. How it manifests: Successful programs have between 1,500 and 30,000 initiatives live in the system. AI helps measure owners to manage the admin by, for example, suggesting business case calculations and sensible milestone plans.

— *Financial impact.* Each measure needs to have an associated financial impact, including implementation costs, calculated according to clear guidelines and based on EBIT or cash. How it manifests: Each initiative has a business case attached to it, and the controlling department has signed off on it. AI helps measure owners make the required calculations and helps the controlling department review them at scale.

— *Reconciliation.* The turnaround program needs to reconcile with the company's P&L and cash flow statement, with no detached shadow reporting. How it manifests: A performance bridge connects the initiative pipeline with the previous period's actual performance and the current year-end outlook; the respective legal-entity owner signs off on each initiative's bottom-line impact. AI helps appropriately identify and size headwinds in the performance bridge, especially for the rest-of-year portion.

— *Attention.* Senior leaders need to have sufficient headspace to challenge the organization and go deep without delegating. How it manifests: Successful programs dedicate and protect entire days of senior leaders' schedules to allow for meaningful and deep discussions of the relevant pressure points. AI helps senior leaders efficiently identify areas to double down on and raise the right challenges for the operative teams.

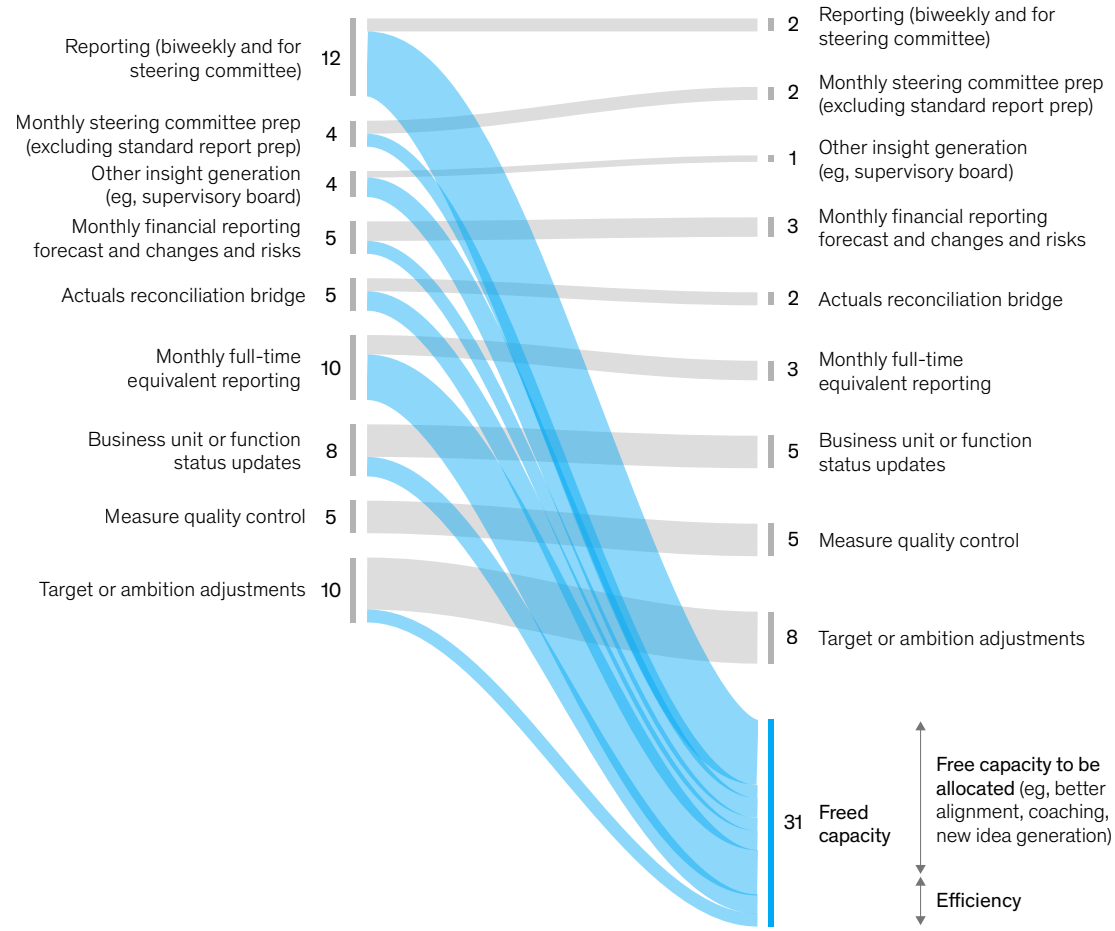
By leveraging AI, the transformation office can keep administration nonnegotiables manageable and nonbureaucratic, essentially removing the trade-off between bureaucracy and impact.

For example, in one case, AI enabled the transformation office to size risks in minutes, answer CEO questions live, flag hundreds of millions at risk in a single cycle, and free up 50 percent of time for proactive risk detection, idea generation, and coaching (Exhibit 8).

Exhibit 8

AI-enabled transformation offices free up about 50 percent of capacity and can give a real execution advantage.

Case study of AI-enabled transformation for a European automotive supplier,
days saved per cycle by transformation lever



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From Portugal to Germany, cost disadvantage pressure weighs on every industrial across Europe, but there is a way to regain competitive success. None of these six turnaround success factors we identified is easy, but all are necessary and increasingly urgent because 45 percent of Europe's industrial companies have an elevated need to transform their operations. Our in-depth understanding shows that restructuring is possible and can be highly effective if carried out in a disciplined, systematic, and constructive European way.

Not all the structural impediments that companies face can be dispensed with by corporate actions; some, such as high energy costs, depend on geopolitical and other external factors. Yet Europe's industrial comeback needs to start soon if the region is to regain a competitive edge.

Europe as a whole stands to benefit from decisive and prompt action that could save and create jobs, grow the economy, and ensure the region remains a vibrant industrial player.

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The authors wish to thank Andrea Queirolo, Andreas Haunreiter, Eike Reus, Johannes Wojciak, Patrick Wetzel, and Timo Kamp for their contributions to this article.

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