

Business Optimization

During Recession: More than Cutting Costs

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A Recession Is a Terrible Thing to Waste. Businesses often see a recession as something painful that must be endured until the economy gets back to normal. Sales projections fall short and “survival mode” kicks in. Expenses are cut, staffing is tightened, programs are scrapped, projections are lowered, fear and uncertainty soar. Yet stories abound about companies that flourish during periods of economic downturn. Intel, Southwest Airlines, Best Buy, Amazon and Charles Schwab grew an average of 30% per year during the recessions of 1980 – 1982, 1991 and 2001, while their counterparts stagnated, contracted or disappeared.

As unprecedented as this economy seems, economic cycles are no different from the weather. Sunny days come and go, as do stormy days. It is how we handle each day with its own set of conditions that shapes our lives in the short and long run. Likewise, long and short-term business success is shaped by companies’ preparation for and response to ever-changing business and economic conditions.

Companies that master business optimization during a recession allow economic forecasts to guide company strategy to competitive advantage by focusing on five priorities:

1. Review and realign market and operational strategy
2. Protect and strengthen your core
3. Spend wisely
4. Remain visible
5. Position for recovery

Review and Realign Market and Operational Strategy. *Don't be caught off-guard!!*

Profitability results from competitive advantage. By definition, a competitive advantage means *sustaining* an edge over the competition with greater sales, margins and customer retention in *any* economic climate. This starts with a clear strategy that defines what business you are in, how you compete in the marketplace and what specific targets you will achieve over time. This also requires a focus on timing. Focusing on strategic timing requires paying attention to economic and industry forecasts; adjusting strategy well in advance of dramatic shifts; and realigning resources, operations and expenditures to the adjusted strategy.

As many companies have learned, a competitive advantage in an expanding market may be disastrous in a receding market if the supporting operational strategy isn't adjusted in a timely way to meet new competitive realities. Classic examples are companies with strategies requiring a lean corps of highly skilled employees. For these companies, “right staffing” in an expansive economy can result in overstaffing, quality compromises and customer service challenges in a contracting economy. Having a strategy that anticipates and prepares for market shifts allows for smooth transitions and sustained competitive advantage by maintaining customer satisfaction, production capacity and profit margins. It puts company management in a proactive rather than reactive mode, and with effective communications may ease employee tensions and fears.



A proactive company would assemble a group of key decision-makers and stakeholders – the board, executives, key employees, suppliers, and advisors; set aside several hours to discuss the company’s current strategy relative to market conditions; then create or revise their market and operational strategies using the following process:

Step One: Market Scan

Examine information about market changes from industry sources. This information is available through trade associations, online sources, marketing companies and consultants.

Review financial statements and sales documents to identify the source of your top 20% of sales. Determine what those customers have in common – demographics, geography, buying patterns, company size, industries and the like. Survey these priority customers to understand their current and shifting priorities, needs, fears, requirements, budgets, expectations, spending habits, perception of your company, perception of competitors and preferences relative to your products and services. In short, learn what, when, where, how and why your key customers buy. Obtain this information in a way that strengthens your relationship with these customers by conveying a genuine interest in understanding and meeting their needs.

Step Two: Value Proposition

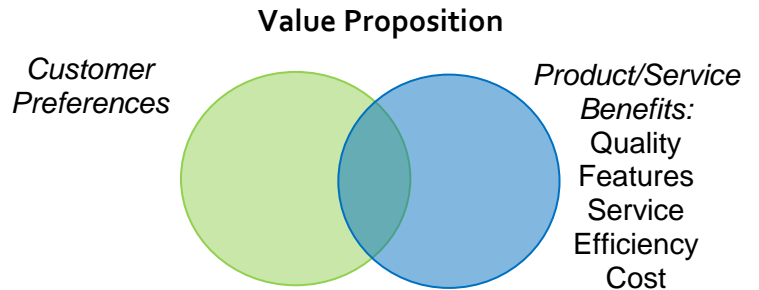
The time honored value equation can effectively guide a reassessment of your strategy.

$$\text{Value} = \text{benefit/cost}$$

This equation reminds us that customers buy because they perceive value and value is enhanced by increasing benefits or decreasing costs.

With so many uncertainties in a recession – how long it will last, how consumer spending will change – many companies respond by controlling what they can – costs. Yet this is only one side of the equation.

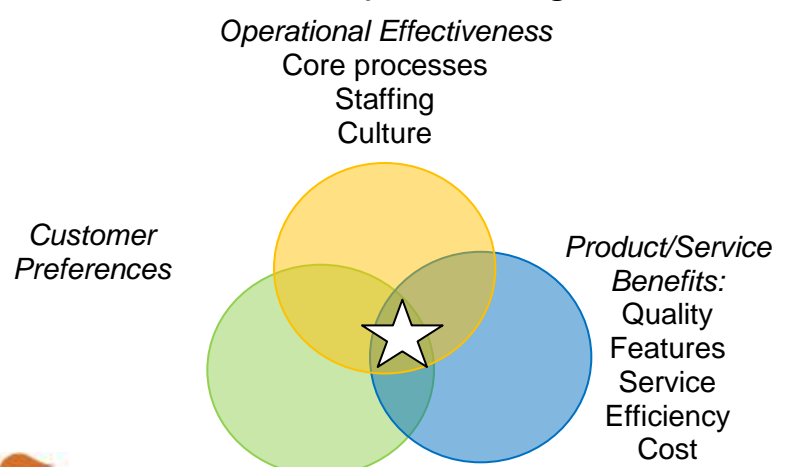
As illustrated below, understanding how the benefits of your products and services overlap with the value the market wants at any point in time helps define your “value proposition” to the marketplace. This is the foundation of your market strategy.



Step Three: Operational Alignment

After determining how your company adds value to targeted customers, assess current operations to assure they are aligned with your market strategy. Ask how your core processes, systems, staffing and organizational culture contribute to or distract from the value your company wants to provide to consumers. Every person, process, technology and other asset that contributes to the customer experience needs to be well aligned, and used more intensively to create value. This may involve better sales calls, more targeted marketing, enhanced customer service or products that are better at helping customers get the outcomes they want. Remember, a recession means doing *better*, not just doing less!

Market and Operational Alignment



Craft your strategy to match where the circles overlap. Consider core competencies, diversification, divestiture, leveraging resources, product and service offerings, unique features, trends, community service and market positioning.

Protect and strengthen your core. During the urgency of a recession, companies often neglect to protect their core competencies. Core competencies are the company's unique strengths that provide the fundamental basis for the company's advantage over competitors.

In the rush to grow revenue, companies may invest precious resources on ventures outside of their competencies. Similarly, in a rush to cut expenses, they may divest or layoff businesses or people that are essential to a core competency. While these actions may provide immediate revenues, those gains are likely to be short lived. Vigilantly protect your best customers, employees, products and channels of production and delivery. Identifying and monitoring the company's core competencies helps ensure that those assets survive budget cuts and layoffs and remain in place to strengthen performance during and through recovery.

Cost reduction is an important part of preserving the core of your business, as long as the cuts promote organizational efficiency and do not interfere with the benefits the company is trying to create for customers, such as customer service or quick delivery.

A recession provides a good opportunity to address organizational shortcomings that had been covered up by strong profits in more expansive economies. In leaner times, cumbersome processes, ineffective decision-making and inadequate skills in key positions become more apparent – and deadly. Similar to the current downturn, the great depression caused a shakeout that eliminated many players that were

riding the wave of investment without having the business efficiency to survive the downturn. Between 1924 and 1927, the automotive industry went from 108 companies manufacturing automobiles in the United States, to 44 companies. In 1929 auto production dropped 55% in a single year. By 1936, the 'big three' (Ford, Chrysler and GM) held 90% of the US car market.

The "big three" used a simple strategy to endure the downturn and dominate the upturn that perhaps they would benefit from reapplying: They produced what consumers wanted using innovative and efficient methods for the times including leveraging assembly line production methods, standardizing components, and structuring innovation. The companies that perished were using craftsmanship, rather than production.

The key to surviving and thriving in and beyond a tough economy is to deliver what customers want with innovation and efficiency. Build these qualities into the company's core operations by creating efficient processes directed with a laser-like focus to the innovations that are most valued by customers.

Spend wisely. The key spending decision for many companies is how to balance short-term considerations with long-term potential.

Use the value equation (discussed previously) to guide spending decisions. Understanding how the company creates profitable value for current and prospective customers helps determine which business activities to invest in, which to maintain and which to cut back. Identify value-adding and non-value-adding activities by following a customer order through the entire delivery process. Removing activities that neither the customer nor the business is willing to pay for saves costs, speeds-up business, reduces errors and increases customer satisfaction. Funding



activities that do add value is essential to driving profitable growth in a prolonged recession.

Research by McKinsey showed that **companies that beat the last two recessions in 2001-2 and 1990-1 actually increased spending in key areas.**

The research tracked almost 1,000 U.S. companies over 18 years that included those recession years. The companies that emerged in the top quartile after the recession increased spending on sales, innovation and marketing during the recession. Another study found that companies that remained market leaders or became serious challengers during the downturn had increased their acquisition, R. & D., and ad budgets, while companies at the bottom of the pile had reduced them. Although this reduced their cash reserves, the companies traded short-term profitability for long-term gain.

Numerous studies show the difficulty of rebounding from non-strategic spending cuts resulting in a loss of visibility, a perceived lack of staying power, reduced quality, product irrelevance or diminished service. At the same time, cash is indeed the lifeblood of business. While non-strategic spending cuts should be avoided, it is essential to manage cash flow and expenses to cover operational demands through the projected end of the recession, since the cycle of cash inflows and cash outflows determine the business' solvency. Carefully monitor, analyze and forecast cashflow, then work out credit /overdraft arrangements in advance of the need. Review and revise collection procedures to decrease receivables aging, consider invoice factoring and establish creative payment terms.

Spending wisely during a recession also means taking advantage of lower priced materials, capital goods, services, enterprises and talent. Be sure these expenditures are aligned with your core strategy for bringing value to this market.

Remember a recession means spending *smarter* not just less.

Remain Visible. A major study by the Strategic Planning Institute on corporate behavior during the past thirty years found that reducing ad spending during recessions improved companies' return on capital. However, it also meant that they grew less quickly in the years following recessions than competitors who maintained or increased advertising.

Companies such as Proctor and Gamble and Kellogg that grew during the Great Depression predicted that consumers would spend if there was a good value proposition and if they felt an emotional connection with the brand. They kept themselves visible to consumers, community and people. Kellogg doubled its ad budget, moved aggressively into radio advertising and heavily pushed its new Rice Krispies cereal. Its rival Post followed conventional wisdom by reducing expenses and cutting back on advertising. By 1933, even as the economy sank, Kellogg's profits had risen almost thirty per cent and it had become what it remains today: the industry's dominant player.

Proctor and Gamble took an innovative approach to creating an emotional connection with their brand that remains a thriving legacy. They sponsored evening shows on the radio to entertain the masses who were looking for any kind of stress relief during tough times. These shows did not focus on P&G products but they were called "Soaps." (Forever Young connected to Camay Soap, O'Neill for Ivory Soap). This is the origin of "Soap Operas" and the foundation for shows like *Celebrity Apprentice*, *The Amazing Race* and *American Idol* with generous product placements. Consider creative ways to direct and leverage your advertising dollars that takes advantage of media, social media, technology and cultural phenomena.



This recession will no doubt repeat the finding that sustained market success requires sustained visibility.

Position for recovery. Sooner or later the economy will rebound for all viable industries. The impact of the recession and timing of recovery depends on the unique characteristics and interdependencies of each company. Whatever the timing, the **winners in the post-recession will not be determined sometime in the future, but while we are still in the midst of the recession itself.**

The winners will be those who meet the two-fold challenge of surviving the recession while preparing for recovery. They stabilize their organizations by strengthening their core business while refining customer expectations, remaking brand identity, streamlining operations, penetrating new markets and ultimately gaining market share during and after the recession.

Once the business becomes adept at managing through any business and economic cycle, it will prepare in advance of a shift. Until this becomes a regular part of business planning, the market and operational strategy for managing the recession will need to be instituted as early as possible during the recession to avoid significant losses. Once in place, that strategy can be built on to prepare for expansion.

As the economy rebounds, the **market goal** is to understand the inevitable post-recession paradigm shift that has reshaped your markets (domestically and internationally) and find your place within it. This requires:

- Paying attention to industry trends through associations, suppliers and networks
- Learning customer post-recession expectations
- Reevaluating the competitive landscape to uncover product or service gaps and opportunities
- Enticing competitors' consumers whose loyalties were disrupted by the downturn
- Seeking alliances, partnerships and joint ventures to enable a quicker response to improving market conditions and capacity to take advantage of opportunities without large up-front investments

The **operational goal** is to build up production and service delivery functions as the economy recovers and prepare to move goods into the sales channel to meet pent-up demand as it is unleashed. This requires:

- Careful matching of services and operations with new customer expectations
- Tracking, monitoring and developing the company's core competencies to maintain capacity to compete and deliver
- Focusing on employee retention as the job market opens up. Employee involvement, development and recognition; competitive pay and benefits; flexible scheduling and respectful, skilled supervision could impact employees' decisions to stay.
- Delivering exceptional customer service
- Drawing on high-quality, low-cost tools and technologies to develop, test and begin to commercialize ideas



A recession is indeed a terrible thing to waste. In his book, *The Great Disruption*, Scott Anthony calls this a period of "Accelerated Darwinism" or "survival of the fittest sped up." Having market and operational strategies that focus on building

value for the customer, investing wisely during the recession and preparing for the inevitable rebound in the economy will make your company "fit" enough to ensure survival well into the future.

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