What do we need to do different in recession?

Depending on who you listen to, the UK, perhaps along with the rest of the world is headed for a recession. Some of the early indicators are already flashing, such as inflation and interest rate rises, and significant pressure for wage increases in many sectors.

Of course this will be a more challenging recession coming as it does off the back of a worldwide pandemic and the impact that has had on supply chains and business profits for example.

So let's consider what businesses need to change as the economy turns. What should they do differently in a recession…?

Actually nothing.

Good business practice is the same in a recession or a growth phase. The only difference is that in a stable economy where the financial pressures are less, businesses and individuals become a bit more complacent. They come to rely on instantly available credit, so they don't chase debts as hard as they should. They are confident that business will come in next month regardless, so they don't look after their customers quite as proactively as they could. So the short answer is that many firms just need to get back to the basics of running a good business and do all the things they should have been doing already.

The problem comes in changing behaviours quickly. If you have been soft on chasing debts for the last few years, it is then very hard to reinforce 30 day terms overnight. If you have developed a passive sales team that just collect and process orders, it is difficult to get them to immediately turn into a proactive and dynamic sales team chasing new sales.

Let's look at a few of the key issues where every business should be focussing their attention as we enter into this difficult period.

CASH

The old saying that 'cash is king' has never been truer. Over the last decade we have seen literally hundreds of new 'banks' springing up. Interest rates have been low, people had confidence to borrow (often more than they should) and would often do so from lenders outside of the big banks and mainstream lenders. A bit short for wages? Often a quick call would see a temporary overdraft increase or a short term loan. You could even borrow money every quarter to spread the VAT bill over three months until the next one was due.

As we look forward we are already seeing many lenders tighten up on their lending criteria. Banking covenants are being checked and challenged when it would only have been mentioned in passing just a year ago. Banks are becoming more direct on tackling hard-core overdrafts (accounts should swing between a credit balance and the overdraft limit, where many just bounce around near the limit all the time). The reality is that the supply of money will get tighter. Easy access cheap money will be hard to find, and running out of cash a much bigger problem to fix.

So what do you do? Plan. Do a cash flow forecast so that you understand when your pain points will hit. This is often when wages, PAYE, corporation tax and VAT hit in the same month, but could be the final part of a big job where you are waiting for the last instalment from the customer, or the 'interest only period' of a loan finishes. Find the blips and plan well in advance to resolve them.

Also, chase debts harder than you have. Over many years we have seen profitable businesses fail because they couldn't (or wouldn't) chase money from customers hard enough. We often hear "But we can't put them on stop as they are a great customer" only to find they haven't paid a penny off their account for the last 4 months! In our book that is not a great customer! Be flexible but be tough.

IMPROVE SALES

Notice we didn't say 'GROW' sales. This is a mistake many business often make as things get tough. They believe that just growing the top line will increase the bottom line. It rarely does. Sales growth often comes at the expense of profit margins and many growing businesses make less money!

The problem is that saying 'Grow sales' is like saying to a Tennis player, 'Play better'. We need to drill down into each aspect of the player's game and decide if attention is needed to their service, their backhand or volley skills, and coach each part individually.

We have a great piece of software that analyses the financial performance of a business and poses various 'what if' scenarios. This looks at what we call the 5 ways to grow your business. Sales income comes from our customers, so we must consider how good we are at winning new ones (of the right type) and how good we are at preventing existing good ones from going elsewhere. We call these the '***acquisition'*** and '***defection'*** rates, and then develop strategies to improve them. Next we consider how often customers buy from you at the moment. Is it once a year, once a month or once a week? Whatever the current average sales ***frequency*** rate, the question is what actions we can take to try to increase it. At the point of a sale there are two further elements. Firstly can you increase the amount that customers buy? This could be from higher ***volumes*** (customer wanted 1,000 letterheads and you persuaded them to have 2,000), a better quality option (They were looking at standard paper and you talked them up to thicker paper with embossed logos), or ancillary products (you sold them business cards or envelopes etc). The final part of the equation is trying to obtain a higher ***price*** so that margins improve.

The key question for any business is…

Do you know your current acquisition rate (how many new customers you win each year), your defection rate (how many you lose each year), you sales frequency (how often on average customers buy), the average value of each sales invoice raised in a year, and the gross profit margin achieved. Whilst you may now some of these the odds are you don't know them all and that they are not reported or managed in any way.

Whilst there are many actions that may overlap (great customer service will help to keep customers, but may also help to win new business) the key is to look at each of the five ways to grow and make sure you have strategies to improve in each area.

The software we use is brilliant for focussing attention on the areas that have the most impact for your business, so if you would like to see your numbers run through the software give us a call.

MANAGING PEOPLE

There are very few businesses that are not reliant to some degree on the number and quality of people they employ. Recruiting the right people, managing and motivating them to do a good job, and helping them develop and progress, are all positive things that any good employer should do. As part of the deal, the employee will also expect a package of rewards that is appropriate to their role, whether just a fair hourly rate, or perhaps company car, pension or other such benefits.

In a stable economy with moderate unemployment the scales finely balance the power between employee (to expect reasonable pay and rewards) and the employer, who expects fair effort and a recognition that the business must evolve and employee arrangements change from time to time. When the economy is volatile there is a risk that high unemployment gives too much power to the employer (if you don't like it we can easily find someone else who will). If there is very low unemployment it can put power in the hands of the employee (or their unions) to demand higher pay, better terms or restrictive practices that hold the business back. Neither is really good for either side, but a turbulent economy causes disruption to the employment market place for all.

What should you do? Same as always.

- Have fair and transparent pay structures that employees can understand.
- Treat people fairly and with respect
- Provide support for employees on wellbeing, childcare or other aspects that can affect their ability to perform at work.
- Train and develop them to be the best they can be. As they contribute more, reward more.
- Be clear on underperformance and have robust appraisal and disciplinary processes
- Say thank you when they go the extra mile, with cards, gifts, cash or just "Thank you"

Whilst long term working relationships are not all about day to day pay levels, recognise that some employees may be struggling to put food on the table and may need extra help.

Are these issues new in a recession? No. But they are much more important when employees can choose to move elsewhere and are being enticed to do so, or where they have a financial need to go for the higher salary even if it is with a terrible employer.

FINANCIAL CONTROL

This is pretty simple really. If you want to run your business well then you need up to date and reliable information. Weekly sales updates and cash reports, monthly management accounts, quarterly cash flow forecasts, a report on the Key Performance Indicators (the points covered in section on 'Improving sales' for example).

When sales are good and there is money in the back, many businesses can be a bit too relaxed on the financial information the get to run the business. When things get tougher, it is crucial to have prompt accurate information so you can see what's going on and react quickly to any changes.

Whilst most clients may be doing some of these things, the harsh reality is that being 6 out of 10 on these issues will no longer be good enough. On these business critical issues you may need to up your game and aim for 8 or 9 out of 10 if you are to survive and prosper over the next few years.

If you want any help on any of these issues, give us a call.

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