

OPPORTUNITIES DURING A RECESSION

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The objective of this report is to identify areas of particular concern for businesses trading in an economic downturn and offer solutions and suggestions to problems that arise whilst trading in an uncertain economic climate.

CUSTOMERS = SALES

Keep your friends close and your enemies closer but you need to keep your customers closest of all. In a recession the market place becomes much more aggressive and competitors will go to extraordinary lengths to ensure survival, this means they will be hungry to consume your customer base.

Customer base growth:

During an economic downturn it is likely that your customer client base will decline in numbers. It is important to track the numbers of customers you are losing to identify trends and explanations for the loss of customers. Your business may lose customers because your business has not responded quickly enough to the new economic reality. You need to assess if your product or service offering needs to be adjusted. It may be your customer base no longer requires all the bells and whistles that we demanded during an economic boom. You could tailor your product and service offering to reduce the selling price and retain customers who would otherwise move to your competitors.

An opportunity to grow your customer base in a downturn arises when a competitor goes out of business. It may be the case that your competitor lost 50% of their sales

and their business became unviable. This means that there is still 50% of their sales available to your business. So if a competitor had sales of €1m that dropped to €500k before it collapsed your business has the opportunity to capture some of this €500k worth of sales.

Another opportunity to grow your customer base in a downturn can arise if your cost base is lower than your competitors. An example of this would be a small home based business that does not pay rent or have full time staff. When this type of business is quoting for work and it has spare capacity it can easily undercut a competitor who has a higher cost base such as rent and a fixed number of staff to pay. In a recession customers will be seeking a lower cost for products and services they purchase and also a more responsive supplier. A small business will be better placed to offer a more responsive service as the customer will most likely be dealing with the owner of the business.

If you need to increase your customer base your business can adopt a more predatory approach and specifically target the customer base of your competitors. If this tactic is engaged be sure to factor in the likely response from your competitors. Depending on the business sector in which you operate you need to compete on more than just price. Offer a benefit that your competitors will find difficult to match.

Customer retention – manage customer expectations

Customers expectations need to be managed carefully especially during a recession.

Customers may take the view that in a recession your business should be grateful for any business it gets and should drop the price of products or services to extremely low levels. In addition they may expect the delivery of products or services at very short lead times. When customers' expectations increase to such a degree it can be impossible for a business to meet such expectations. Your business may be in particular difficulty and be desperate for sales so it may endeavour to meet unrealistic customer expectations, this is an extremely dangerous path to tread. Inevitably your business will fail to deliver what your customer has demanded and you may end up not being paid in or full or worse, not being paid at all. It is better to refuse a sale to a customer with expectations that are highly unlikely to be met than to accept the sale.

In order to manage customer expectations you need to clearly communicate to the customer the process of the work required or how products are produce and delivered. If a customer wants delivery of a bespoke piece of computer equipment if five days and the parts needed to produce the product take ten days to be delivered from Japan then their expectation cannot be met. Most clients will accept a valid explanation. The better informed the customer is the better your ability to narrow the expectation gap between what the customer wants and what the customer can realistically obtain.

Customer referrals – ask and thou shall receive

Obtaining business by way of referrals is one of the best and cost effective ways of growing your customer base. The more often you ask for the referrals the better chance you have of generating new sales leads. You should also offer to refer your customers businesses if applicable, this is a win win situation. When you obtain a new customer through a referral you should be exceptionally attentive to their requirements as their opinion matters to both your business and the person who referred them to you. Each new customer has the potential to generate a least two new referrals for your business so consider this as you deal with your entire customer base.

Customer contact – frequency – avoid “and who are you?”

During a recession your competitors will be seeking ways of stealing your customers. To avoid your customers moving to a competitor you need to be particularly attentive to their ongoing requirements from your business. One method of creating loyalty is by remaining in continuous contact with your customer base. By having regular communications with your customers you will be aware of the issues that are affecting them and how you can modify your product or service offering accordingly. You want to ensure that your customers are aware of your interest in their business. Your customer needs to know you are actively engaged in assisting them above and beyond that of any potential competitor would be willing to do. You do not want a situation where you customer can hardly remember who you are when you contact them, this is the “who are you?” syndrome and leaves your customer available to the offerings of competitors.

Customer communication – by phone / face to face / e mail / text / newsletter

Expanding on the concept of customer contact you need to identify the most appropriate method of contact. There are many options available, some more efficient and effective than others. The phone is one of the best as it is quick, avoids travel and is instant. You need to be conscious of the fact that customers may not be inclined to chat idly on the phone so you should have something of interest to communicate with them. It may be a new product that could be of use to them, it may be a filing deadline they need to be aware of, whatever the reason for the communication it needs to have a benefit for them. Face to face contact can increase the impact of your communication, a lunch is nearly always greeted favourably. E mail is quick and effective, especially if your customers are not inclined or too busy to meet up or talk on the phone. Newsletters often produce a mixed response and some industry sectors are more suited to this type of communication than others.

CASH

It used to be the case that cash was king, in a recession cash is promoted to emperor.

Businesses need to ensure that they have sufficient working capital to meet the requirements of their business. The best way to control cash is to use a rolling cashflow forecast to facilitate active cash management.

Capital

The amount of monies injected into a business represents its capital, many businesses particularly in the SME sector suffer from a lack of capital. In a recession a business that is lacking in appropriate levels of capital is particularly vulnerable. Each business needs to assess if it has sufficient capital. If a business lacks sufficient capital it needs to seek out ways to deal with its deficiency. It may involve an injection of funds from the owners of the business or if that is not an option seeking out private investors to inject capital in the business for an equity stake. If neither of the aforementioned options are viable then it may be a matter of retaining as much of the profits in the business going forward as possible. Finally it may be an option to obtain debt capital from a financial institution by way of a medium or long term loan. The obvious downside to debt capital, loans, is it attracts interest payments that add to the cost base of the business. If the injection of funds is used correctly it should impact on sales thus creating enough profit to cover interest charges.

Cashflow forecasts

If you are running a business without cashflow forecasts you are hindering your ability to control the business effectively. Cashflow forecasts can be time consuming to produce so you need to identify how accurate and detailed you need them to be. A basic cashflow forecast is better than none at all. It is easier to forecast the outgoings of a business as you have control over these, so a simple list of all the payments due each month is a starting point of any cashflow forecast. By listing all the direct debits, standing orders, loan repayments, lease repayments, payroll, tax payments, you will at the very least identify the amount of cash that needs to be generated each month to cover all the outgoings.

Monies due in may be based on best estimates of prior trading periods. If you have debtors an up to date aged debtors listing will help identify who owes what and your credit control contact with debtors will establish who will be paying their debts and when.

The cashflow forecast will give an indication of future bank balances that should enable the business owner to plan accordingly.

Debtor & Creditor Days

If you trade on credit you need to know how to calculate debtor and creditor days.

Debtors days is the length of time it takes for your customer to pay you.

Creditors days is the length of time it takes for your business to pay its suppliers

If your terms of credit to debtors are 60 days and your debtor days is running at 120 days then obviously your business has a serious problem. It is only by monitoring debtor days will a business be able to take action to stop the situation deteriorating.

Conversely if the credit terms on offer by your creditors is 30 days and your creditors days is running at 90 days your business is in danger of losing credit facilities with suppliers. This could in turn result in product not being supplied by creditors until payment is made up front.

Debtor days is calculated as follows: $\text{Debtors} / \text{Credit Sales} \times 365 = \text{debtor days}$

Creditor days is calculated as follows: $\text{Creditors} / \text{Credit purchases} \times 365 = \text{creditor days}$

Payment risk Sole Traders Verses Limited Companies – PG option

If your business is dealing with limited companies it can be beneficial to insert into the terms and conditions that the directors/owners of limited companies will be held personally liable for the debts of the business in the event of liquidation. If the customer refuses to sign up to such a condition then it is a judgement call on behalf of the business owner whether or not to do business with the customer.

Credit control

Credit control should be given priority during a recession. If the business does not have a documented credit control policy it should endeavour to produce one. The credit control policy document should cover the following:

- The credit application process
- The procedure for setting credit limits for customers
- The procedure for the collection of outstanding monies from debtors
- Once the credit control policy has been finalised it is important to adhere to it as it will only lead to erratic results if it is not.

Cash Management – How to get out of the red

- Identify items of expenditure that can be deferred – e.g. capital expenditure
- Contact your largest suppliers and request extended credit terms
- Request deposit payments from new customers
- Request payments on account from slow paying customers
- Use staged payments for major overheads e.g. insurance

CONTROL

Groucho Marx said, “It’s easier to spend two dollars than to save one.” In business this is also true only the multiples are larger. Control needs to be exercised over costs, business operations and KPIs

Cost Control

Cost control is a system that tracks and monitors costs. This is a most basic function of any accounting system. By recording the costs incurred a business can evaluate if costs are at an acceptable level and engage in cost containment and cost cutting where necessary, see below.

Cost Containment

Cost containment refers to maintain particular costs within particular parameters. An example of cost containment would be to ensure that payroll as a percentage of sales does not increase above 10%. Therefore if sales drop payroll will need to decrease to ensure the percentage of payroll to sales remains constant.

Cost Cutting

Cost cutting involves the reduction of costs that are incurred by a business. It involves identifying costs that can be reduced by seeking discounts from suppliers or seeking alternative suppliers or substitute products or services. An example of cost cutting would be an expense for staff travel and subsistence that needs to be reduced by requesting that staff fly economy class and staff at budget hotels.

Business operations review

A downturn in business offers an opportunity to completely overhaul how your business is conducted. A natural consequence of a recession is that business slows down, this means time can be available to conduct a review of your business. A detailed review of how the business operates can reveal issues that might have gone unnoticed in busier times. It may be possible to eliminate processes, reorganise staff duties and streamline operations to create a more efficient organisation.

KPI's – know your numbers

Key performance indicators allow a business to be monitored and remedial action to be implemented where necessary. Every business can produce KPI's unique to their sector however some basic KPI's relevant to most businesses would be:

- Net profit margin
- Gross profit margin
- Breakeven sales
- Debtors days
- Creditor days
- Current ratio
- Stock turnover

OPPORTUNITIES IN A DOWNTURN

Murphy's law states that anything that can go wrong will go wrong, in a recession

Murphy's law is usually proved correct. Although trading during a recession is tough there are opportunities if you look carefully enough.

- (1) Reduce costs
- (2) Take advantage of downtime
- (3) Increase market share
- (4) Recruit top class staff & off load passengers
- (5) Implement changes to improve efficiency
- (6) Marketing Passive / Active - Selling
- (7) Review product/service offering
- (8) Merger / Take over
- (9) Outsource
- (10) Avoid/Eradicate complacency