Advancing the business in the down market

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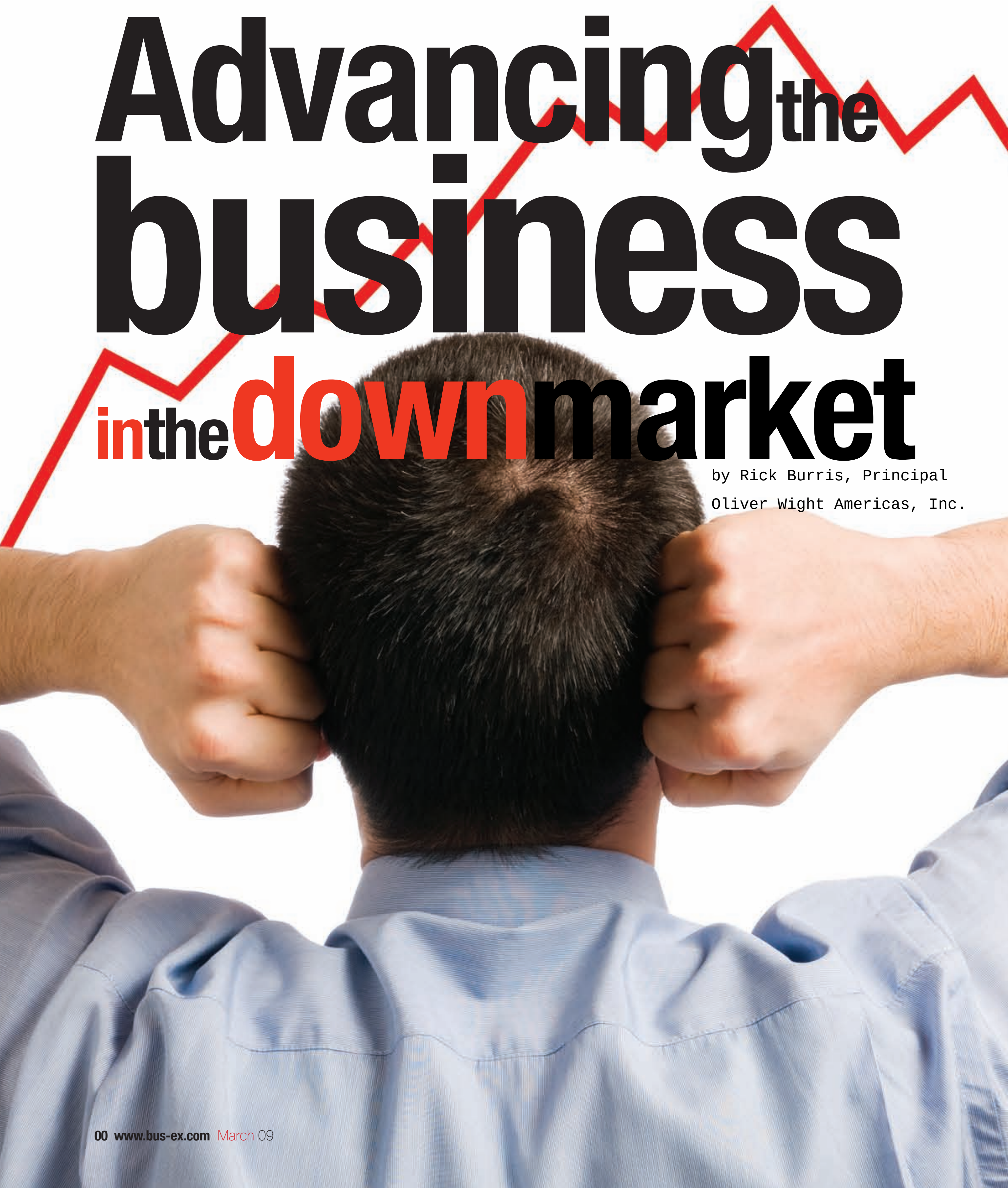


In a downturn, forward-looking executives focus not only on survival, they also prepare the business for recovery. Article three in this series on effective executive management during an economic downturn describes the strategies and practices that business leaders must deploy to achieve this

Introduction

Economic downturns are accompanied by the failure of weak businesses and ineffective executive teams. Meanwhile, other businesses are positioned for growth by executive teams that have the foresight to make the best choices that will lead them into the inevitably better future.

In article two, we discussed methods for eliminating work and complexity from the business to reduce costs and maintain profitability during an economic downturn. Assuming this has been successfully implemented, it now becomes the senior executives' task to advance the business in spite of the limited opportunities provided by the economy.

Essentials for advancing the business

Previous economic downturns have driven some companies out of business while others not only survive but thrive in the highly competitive environment. Oliver Wight has worked with many companies that have achieved success, and we have observed a common denominator among them; the successful companies have a continuous executive process for anticipating the future and planning activities to take advantage of the predicted environment. This process, like all forecast-based systems, is not successful through clairvoyance. Success is due to the routine review and adjustment of marketplace forecasts and the attendant actions for driving the business forward.

In successful companies, two dimensions of action are always present. First, they manage the business in a manner that keeps the income statement profitable, and they manage the balance sheet to produce cash for flexibility in their asset pool. Secondly, they take advantage of the time of lower activity to address weaknesses in infrastructure and infrastructure processes to produce lower operating costs, better customer service, and increased ROA.

Financial management in economic turmoil

Every company closely manages its finances during an economic downturn. The least effective among them, however, make it an activity of the finance department alone, with every expense, no matter how minor the amount, having to be approved by the controller or even the CFO. In contrast, the more effective companies have financial management as part of the overall executive management process where business and expenditure plans are continually assessed and adjusted in an integrated fashion and where all decisions are made concurrently and with full integration.

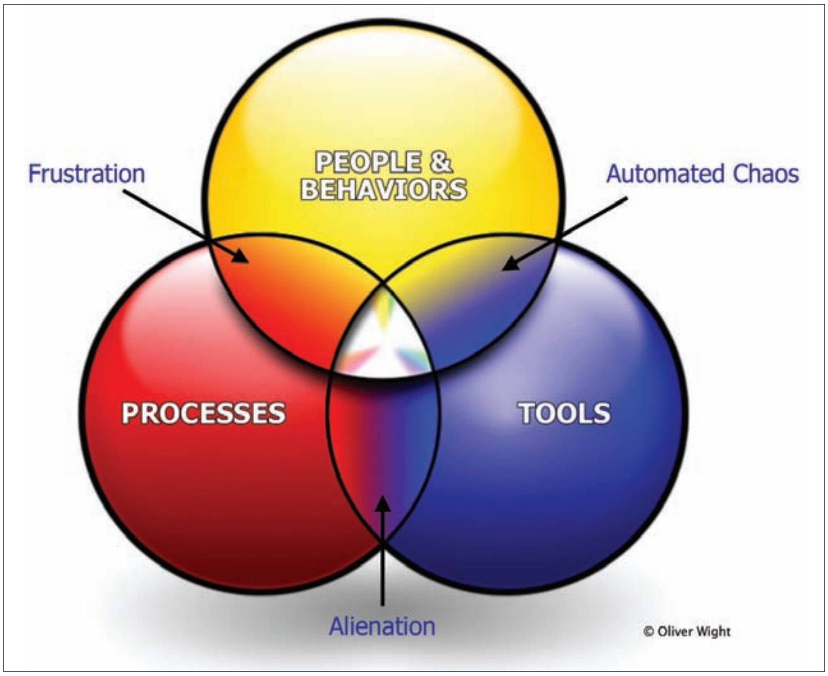
The poorer systems tend to work on a first-come, first-served basis. This often results in important activities being curtailed simply because "this month's expense funds are depleted." Conversely, the better systems demand that all management make expenditures to accomplish goals and objectives that are mutually developed, well communicated, and deployed. Executives are tasked with achieving results with a well-defined and approved set of resources, following a process with many interim milestone accomplishments to ensure cost and benefits are meeting expectations. Reviews are continuous and plans revised as results are assessed.

Another area where successful companies excel is in credit management. The offering of terms can be a tool for success or a road to disaster. The only thing worse than not selling is selling, delivering and not being paid. We often see companies offer special terms to drive short-term demand. This often results in pulling demand forward, rather than providing a true lift. These terms are also most often accessed by customers with liquidity issues and often lead to bad debt surprises within a few months.

A one-size-fits-all credit policy may also not be the best decision during an economic downturn. Many companies realize that a portion of their customer base will not survive it, but they spend little time assessing which customers will fail and which will be a part of their growth once the economy or market returns. Additionally, special terms for new, healthy customers can be a great tool for capturing market share from competitors who cannot afford to offer better terms. The best companies incorporate a more detailed review of credit and collections into their executive management process during economic uncertainty to manage risk and exploit opportunities.

The final dimension of cash management relates to the supplier community. Economic turmoil drives all companies to reassess their suppliers' performance and selling parameters. The best companies use the leverage of downturns to drive better supplier support of their strategies. The least effective companies simply demand price concessions, which can further weaken their supplier base.

The best companies work with suppliers on lead times and minimum order quantities. Shortening the replenishment cycle and moving toward "lot-for-lot" quantities against demand will have a much greater effect on cash flow and inventory reductions than any price concession. This is the ideal time to find the suppliers whose internal processes best match up with your needs for quick delivery in the right quantity.



Addressing weaknesses in infrastructure processes

The major difference between companies that succeed and those which fail in tough economies is their focus on improving the performance of their internal processes, systems, and workforce. The companies that most frequently fail typically reject every operations improvement project as being unaffordable during their first step in downsizing for the lower demand. While all expenditures need to be assessed, wholesale rejection has many unintended consequences.

We use this model to illustrate the potential consequences. For example, the elimination of improvement projects is often coupled with a downsizing of the workforce. This sends a number of negative messages to the employees who are left to accomplish their department's responsibilities. First, it may lead to a wrong impression that the executives don't see a long-term future for the company. Second, eliminating funds to refine or replace tools or provide training on these tools can cause additional frustration and alienation. This all leads to resentment within the workforce at having to do more work (perceived due to the layoffs) with less than adequate resources to effectively perform their tasks.

Determining what needs fixing and prioritizing those repairs is a continual executive dilemma. Trust is not always earned by those sponsoring the improvements because prior projects have failed to deliver the benefits anticipated when the resources were authorized. An example of this is in the area of ERP systems. Many companies have invested in these systems over the past 10 years, yet very few business organizations are utilizing the tool to its total capability.

A chapter of The Oliver Wight Class A Checklist for Business Excellence is dedicated to planning and control processes and systems. Even though there are significant, tangible economic and customer service benefits to meeting Class A standards, few companies take the time and effort to meet these standards. This makes little sense, especially when the investment to become Class A represents a small percentage of the total investment in software and implementation. Objective measurement of sustained performance and subjective measurement of behavioral norms are the basis for achieving Class A certification.

Informative and credible performance measures can identify repair needs and help to prioritize the necessary resources for the fixes. However, we still observe many successful companies measuring the wrong parameters or measuring them in a manner that produces a number rather than actionable information.

Senior management is still dealing with agenda-driven filtering of data and measurements. A new focus in this area is very valuable in economic turmoil because lean, reliable processes are the only kind affordable over time. Effective performance measures include all processes in a company. They include the following review attributes:

- Volume processed
- Productivity – resource divided by volume
- Planning effectiveness – ability to predict and adjust to the future
- Execution performance
- Schedule
- Cost
- Quality
- Velocity
- Escapements - individual occurrences that had an unusually large deviation from one of the four above measurements that could be hidden by simply looking at an average.

Once these measurements are in place (with at least a year's history), the best companies calculate the cost of substandard performance, the tasks required to bring the performance into a targeting range, and an estimate of cost and time to accomplish those tasks. All substandard processes are then prioritized based on economic value or customer service improvements (all of which are expressed in economic value terms). Resources are then set aside for these initiatives that have the greatest potential return or value on the financial plan.

An example from my own industry experience relates to a major ERP implementation. After a year of effort, our market turned downward to the tune of 22 percent. While we had many millions budgeted to modify/configure the ERP package we had purchased, we made a decision to curtail all tailoring efforts.

At the time, there were 1334 requests for software changes in the pipeline. We told the employees and middle managers that they had to learn to use the software "as is". However, realizing that there were actual deficiencies in the software, we established an appeals board composed of three of our best project managers (this quickly became known as the "murder board" by the workforce) to review the 1334 changes. Only 56 items were approved by the board, after which we insisted the software supplier fix them as deficiencies. They fixed 55 at their cost. In the end, we achieved Class A using the vanilla software at about eight percent of the cost of the modifications. Insisting on behavioral changes instead of software changes made the difference. This is often the case with many processes.

Conclusion

In an economic downturn, advancing the business means carefully managing both the income statement and balance sheet to ensure resources are available to service the remaining demand in a way that gives shareholders and stakeholders confidence in the future. Continuing to repair any broken or underperforming processes creates efficiencies for the short term and a foundation for exploiting market opportunities that will arise from competitor attrition and from the opportunities created by the eventual economic or market recovery.

In the final article of this four-part series about effective management in an economic downturn, we will discuss the strategies and methodologies for anticipating and exploiting the eventual economic recovery. ■

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