Recession Planning: Hope for the Best, Prepare for the Worst

Is the U.S. Economy headed for a recession? The economic signals are mixed. Here are four considerations that will help manufacturers get ready no matter which way the wind blows.

Key Takeaways

- Economic indicators are mixed. How can manufacturers prepare?
- What do companies that successfully weather recessions and emerge stronger when growth returns do that other companies don't?
- What are the top four priorities in the next slow growth period?

Over the course of my career I've worked through a fair number of down cycles. I've seen some companies get into serious trouble. And I've seen others make smart and decisive moves that enabled them to get through the slow times and come out strong when growth returns.

The difference comes down to speed and agility.

When business slows down leaders often fail to react early enough and dramatically enough. During times of uncertainty you should assume that the actual situation on the ground is much worse than you think it is and take – not delay – the appropriate actions. If things turn out better than expected, then you're pleasantly surprised. If they don't, your company is prepared.

The most recent economic red flag is the Institute for Supply Management's manufacturing purchasing managers index, which fell to its lowest level since June 2009 (an auspicious month). While the U.S. unemployment rate hit a 50-year low, consumer spending is flat, the U.S.-China trade war drags on, consumer confidence has dropped and construction spending has been trailing the previous year for 10 consecutive months now. The fact is no one really knows what it all means or what the fourth quarter or next year will bring.

Whatever happens in your markets, cash flow should always be the primary focus during periods of stagnant growth. Inflexible cash demands – supplier contracts, debt payments and payroll – can slowly strangle a business. Maintaining financial viability depends on how quickly the cash generation aspects of your business are able to react to any demand changes. Again, it's all about speed and agility.

If business slows down for any reason – in just your markets or across the wider economy – these should be your top four priorities:

1. **Don't Take Your Foot Off the Gas.** Continuing to drive the topline must remain a priority when growth slows, but you may have to change tactical priorities. That starts with giving your sales engine a tune up.

For example, during periods of growth customer service will often falter. Find out how well you're actually performing today with your key customers. What could you be doing better, or differently?

Next, look at your sales channels. If demand slows, think about what impact that will have. Which channels will contract the most? Which ones could grow? Are their any new channels, like web sales, that warrant more focus.

2. **Double Down on Operational Efficiency.** You can't let a slowdown in demand derail your productivity improvement plans. How fast and how efficiently your company converts raw materials to finished goods is how you stay agile and react to up or down fluctuations in demand.

Slower revenue growth will lead to tighter budgets. That means you will have to be more strategic about business improvement projects and priorities. Evaluate your current plans and resources. Ask which investments will yield immediate gains? Which ones will enable longer term strategic gains?

Apply the same filter to your capital investment budget. You will need to be more frugal about your investments to protect cash, but don't turn off the taps entirely. In a slowdown the ROI and payback periods will drag out. Companies that completely cut off spending during down times always come out more slowly when growth returns.

3. Protect Your Working Capital. Accustomed to growth, we see many manufacturers operating with too many assets and too much inventory. This excess could leave you exposed if demand weakens.

Keep pushing sales but don't hesitate to reign in any optimistic sales forecasts. In tight times you can't afford to let unrealistic forecasts lead to excess raw materials or finished goods inventory. Make sure your S&OP process scrubs demand forecasts, removing any excessive optimism.

Instead of waiting until demand tapers off, now is the time to start working proactively with suppliers. Review supplier agreements and talk about the potential need to slow down the flow of incoming raw materials and parts. If lead times are long because of global sourcing, that's all the more reason why you should start planning now.

The same thought processes should be applied to your asset base. How much outside warehouse space are you using? How quickly can you get out of it in a slowdown? Looking at your manufacturing footprint, where will it make the most sense to idle lines?

4. **Hold onto Your People.** Cutting payroll is the kneejerk reaction that manufacturers have historically taken when demand drops and they need to maintain margins and cashflow. But these are different times.

In today's labor market companies are already running fairly lean. Manufacturers are having a hard time filling job vacancies from the entry level on up. You will have to find creative ways to hold onto the people you have now, especially those with the most in-demand skills.

During the last recession in 2009, one of our clients kept most of its employees on the payroll – welders specifically – with limited work schedules and special projects. The company's leaders knew how difficult and expensive it would be to find and hire folks with those skills when growth returned, which it inevitably did.

Those are four key areas to consider in preparation for slower growth. We're now in the longest running expansion in U.S. history, and good times never last forever. That has everyone a bit spooked. The trade war with China and political sideshows aren't helping matters. While the economic indicators are somewhat mixed, there is a general trend toward some kind of correction. Now is the time to get ready.

Would you like some additional reading on scenario analysis? TBM supply chain experts, Brian Cromer and Ken Koenemann, recommended some actions you can take now to increase agility and ensure a rapid response to get ahead of whatever comes your way.

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