What Should I Do Today? In Six Months? In Two Years?

Summary

A company's response to the crisis will be defined by whether it has made preparations long before it hits. The first thing firms need to do is assess how prepared they are for the recession. If the company has diligently laid the groundwork and meets the criteria set out by IESE Prof. José L. Nueno, the first six months could be a good time to launch new products before demand falls sharply. And at the one-year mark, firms looking to buy retail space could pick up some bargains as sites previously priced beyond their price range may now fall within it. These are a few of the opportunities available to well-prepared companies to gain the few advantages a recession can bring.

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In one of the few recent academic studies on marketing's usefulness when a downturn hits, Srinivasan, Rangaswamy and Lilien (2005)[1] revealed that a review of the existing literature yielded only three articles, all published prior to 1979. This may not be surprising, given that companies often slash marketing budgets when a recession hits. In short, the existing literature does not provide much guidance as to whether one should increase or decrease the marketing spend during such downturns.

The official definition of "recession," according to the U.S. National Bureau of Economic Research, is not very helpful for our purposes: "A significant decline in economic activity spread across the economy, lasting more than a few months, normally visible in real GDP, real income, employment, industrial production and wholesale-retail sales."[2] These conditions are clearly present in 2008. But the recession's impact will vary depending on the sector the company operates in, its geographic presence and the depth and duration of the downturn.

At the end of the day, though, a company's response to the crisis will be defined by whether or not it made preparations long before it hits. If a company meets some or all of the following conditions, it could adopt a proactive role and exploit what little positive ground there is during the recession. If not, adopting a more defensive approach is the best recommendation.

There are at least five crucial conditions to be met.

- The first is being able to precisely identify the beginning of a recession. Few can perceive "the edge of the abyss"; it is simply an innate ability. The literature is unanimous in that academic experts are not much help in this respect. Academics' forecast models fail and scholars cannot measure the impact of the recession once it is under way, nor interpret the nature of crises. However, companies that succeed in capitalizing on crises cannot afford to make these mistakes.

Take the recession's catastrophic impact on the Spanish real estate industry, for example. Property developers failed to detect the downturn that was just around the corner. The same is true of the banks that financed property developers. While some banks purchased properties a few months too early for prices way above current market levels, others saw the writing on the wall and offloaded real estate assets before the bubble burst.

- The second condition is to have a cash-rich balance sheet going into the economic downturn as a result of good management during the preceding up-cycle. The capable and committed managers of such companies typically share the mission of capitalizing on the crisis even though its gravity suggests otherwise. As Jack and Suzy Welch stated in their Oct. 2, 2008 column in *BusinessWeek*:

"Plan as if the downturn will be longer and harsher than you think. Look, it's natural to want to inflict as little pain on your organization as possible, cutting back incre-

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mentally to protect jobs and projects for as long as possible. But in a rocky environment, timidity can be very risky. By contrast, if you take a more aggressive approach to costs, there's almost no down side. If the economy really tanks, you'll be one of the few prepared companies. If it's better than predicted, you'll be in a better position to leverage the up side."

The pragmatism of this recommendation touches on two realities. The first is that recessions tend to require more management, not less, as they present more complexities than a growth period. And if your company wants to exploit your competitors' timidity to capture more of the market, you will need to count on your best managers.

You will also need to complement your internal capabilities in terms of human resources. The most capable staff is far more accessible during recession cycles, particularly if you are an employer that demonstrates commitment, decisiveness and the willingness to take action in a downturn.

- The third condition depends on having diligently selected the market sector where you compete prior to the downturn, especially if you have developed a strong position in one or more segments. In consumer markets, the fiercest competition during downturns comes from own-brand labels. When operating in categories where the share of the company's own brand is normally low, an absence of sufficient industrial capacity or lack of leadership in innovation suddenly contributes to greater margins that provide the necessary resources and focus attention on overcoming a recession.

Although it is almost unfair to cite this example, something similar occurs in cash-poor markets with little product differentiation and high competition because circumstances do not improve when a recession hits.

- The fourth condition involves ensuring geographical diversification because, when a crisis hits, some markets stagnate while others thrive. Until now, local players operating in mature markets such as Europe prospered as they capitalized on know-how and focused on serving their growing domestic markets where they held historically significant market shares. The current recession has put an end to this. Emerging markets have an emerging middle class; there are opportunities for companies making products and services for these new consumers and their suppliers.

- The fifth condition is to have a record of excellent execution. If a company has not successfully launched products under favorable market conditions, built notoriety and customer preference and acted as a price leader rather than a price slave, how can it expect to emerge unscathed when consumption slumps and competition intensifies? The company must have previously developed channels that allow fluid access to the market and have efficient, disciplined and direct methods to maximize that fluidity.

What can be done today, in the next six months and in the next two years to strengthen your company's position during this recession?

What you should do today

It is important that your entire organization be crystal clear on the true state of the current market and the company's position in light of changing priorities. In order to tackle this, all available data that provide a response to three questions should be shared:

Who among the competition is best prepared to emerge as the market leader after this recession?

What is at stake if your company were not to emerge as the market leader?

What does your company need to do to keep a rival from emerging from the crisis as the market leader and ensure that your company emerges as the clear winner?

To effectively respond to these questions, management needs to evaluate how prepared the company is in key areas. It is essential to establish clear expectations about the duration and depth of the crisis and translate that into the effects on business. Additionally, the management team must be clear on how to act if the crisis is shorter or longer than expected.

This analysis should include a review of historic marketing data (for example, innovation, success rates in product launches, The first six months of a recession tend to be the most difficult, given that producers and consumers are struggling to learn new behaviors.

the company's position in market segments, its rating in brand notoriety and brand preference). The company needs to carry out this exercise and then repeat it for its biggest competitors. It is also crucial to evaluate your needs in terms of human resources and identify your weaknesses.

This phase should be confidential and executed by a select group of managers. Resulting data should be shared with members only. In conclusion, you should make a first diagnosis as to whether the company is prepared to actively pursue new opportunities in the market or assume a more prudent and defensive position.

What should be done in the next six months?

The first six months of a recession tend to be the most difficult, given that producers and consumers are struggling to learn new behaviors. Demand decreases the most during this period, unleashing emotional and calculated responses from competitors. Examples of this include predatory promotions and sales, price wars, clients making impossible demands, late payments, and clients who disappear or defect to other suppliers. However, once the first quarter following the decision to be proactive has ended, some opportunities begin to arise.

Lower demand favors new product launches, especially if you have a good track record in innovation. Competitors tend to be more conservative during downturns, so there will be fewer competing product launches. In addition, manufacturers' advertising efforts are harder to justify during recessions unless they accompany a product launch. Retailers know this and are more willing to listen to companies with a history of successful product launches as a way of boosting flagging traffic levels at their stores.

Mass-marketing campaigns continue to be the most effective way of whetting wary consumers' appetites and generating sales. It is easier to achieve rapid referencing and get hold of the right media and logistics channels to support the product launch when competitors are less active.

As margins are squeezed, companies may be tempted to cut their advertising budgets - an essential variable cost. Proactive companies need to capitalize on this and invest aggressively. First of all, advertising is essential to a product launch. Secondly, media costs fall due to the drop in demand from other companies that do not have the will or the means to advertise. This decreased demand translates into lower costs for those who continue to advertise, as well as highly attentive service from hungry marketing communications agencies.

In the absence of rival investments, companies that continue to advertise can monopolize consumers' attention. This is patently impossible during favorable cycles, when there is usually a high level of advertising saturation. Recent studies show that during lean periods, marketing communications agencies are more effective if they prioritize their efforts toward proactive companies with attractive products and services. This seems only logical, given that these companies will probably emerge as market leaders after the recession.

It is also important during these first six months to review creativity and formatting. Consumers' situations and the market will have changed, and communication will almost certainly need to be adapted to respond to this. Reviewing sales policies, incentives and conditions with retail outlets is also very important. In fact, innovating sales systems and point-of-sale follow-up procedures during recessions have proven more effective than the "stand-alone" launches mentioned above.

What should be done in the first year?

When the recession approaches the one-year mark, tough conditions can create further challenges and opportunities. The first challenge involves diminishing margins, as competitors get trapped in low-cost models and begin to wage price wars or simply suffer from the slump in demand. Companies that operate in more favorable currencies and enjoy lower labor costs and other perks also represent a threat. It costs these companies less to capture market share during recessions than when the market returns to normal.

Toward the end of a recession's first year, increased competition begins working on two key resources that are usually not so liquid during upturns: staff and real estate. In preparing for the second year of a recession, you can recruit high-caliber professionals who are usually more reluctant to move during other cycles. These are people whose salaries tend to have a variable component based on results. When a recession freezes or lowers their income and their ambitions diverge from

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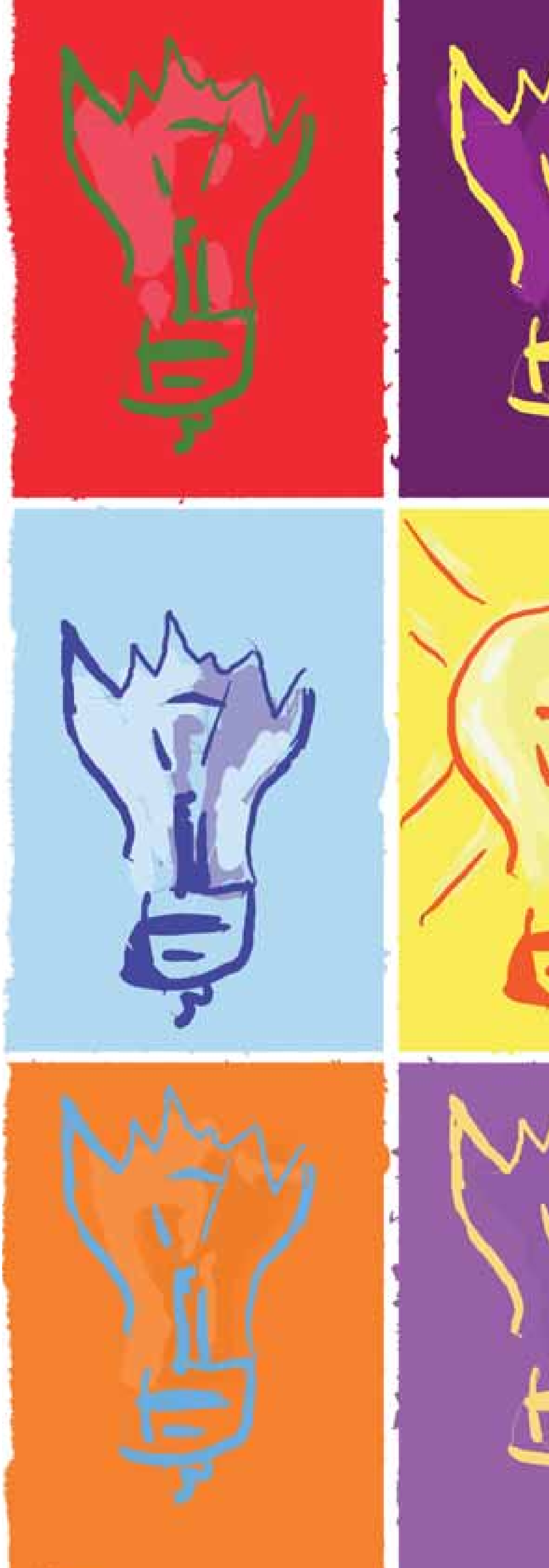

those of their employer, they can become restless and decide to move.

If a proactive company uses retail outlets in its distribution channel or has ever considered adding or migrating toward them, this is the moment to do so. Commercial spaces that were either not on the market or priced out of the company's price range will begin to pop up after the first year of a recession.

As a result of voluntary and involuntary vacancies, some of these spaces could represent a great chance to occupy unique locations. Since more commercial spaces become available in secondary zones than in prime locations, it is important to emphasize that during recessions one should buy in areas densely populated by robust commercial neighbors in order to eliminate consumer resistance and create traffic.

Conclusion

The conditions that allow companies to capitalize on recessions must be cultivated and created before a recession hits. A serious downturn is the moment of truth, where we find out whether we have done everything we needed to do, and how well. The prize does not always go to the hardest worker. Nor does meeting the five conditions mentioned above ensure success in a profound recession or crisis, where the rules of competition are in flux. More consumers opt to abandon categories and service models during recessions than at any other time and they do so regardless of the management's excellence or commitment to the customer. In essence, they are apt to confuse the best-prepared companies with those that entered the market before the actual crisis hit. ■

1. Srinivasan R., Rangaswamy A., Lilien G.L., "Turning Adversity into Advantage: Does Proactive Marketing During a Recession Pay Off?" International Journal of Research in Marketing, 2005.

2. Definition according to the U.S. National Bureau of Economic Research.