A CEO's ultimate task: Bracing for the Downturn

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Businesses fail because people fail to recognize the signs that always appear to herald a change in the future economic environment.

There are signals that are almost universal in every industry and the ultimate responsibility in bracing for a downturn lies with today's business managers. For many businesses over the next several months, there will be no second chance. Unfortunately, a number of chief executives who are guiding companies today have never experienced a severe business downturn.

Continuous planning changes are needed as a company continues to operate. Principals must be aware of changes in the economic environment and in the trends of their particular industry. They must be willing to incorporate those changes into the road map of the company, regardless of how painful the changes may be.

The failure, inability or unwillingness of a principal to recognize the changes and more importantly, the unwillingness to take corrective action when changes are needed, are the overwhelming reasons why a majority of once-successful companies encounter problems that ultimately can lead to serious financial problems and, eventually, failure.

In some instances, the company‰¥ús backlog of orders may begin to deteriorate, resulting in a decrease in volume. But the company continues to operate at the same level of expense. Executives become accustomed to a certain level of overhead to support an image and often simply refuse to react to obvious signals that require immediate adjustments.

Over the next few months, principals and CEOs of successful companies should take a look at the immediate future of their companies and be prepared to make changes.

One of the most frequent mistakes executives make is to put off facing difficult issues. Scaling down a company is often painful. As a result, it is usually much easier and often more effective if the financial projections are prepared by the company in conjunction with an independent third party.

Problems must be addressed immediately, rather than wasting energy avoiding the problems. Although solving problems is painful, often what appears to be the most difficult task is ultimately the easiest in the long run.

A number of businesses that are or appear to be thriving today will, in fact, fall on difficult times over the next 12 months. Some will even cease to operate because principals simply refuse to take the time to look into the future and take decisive action.

Whether senior management constructs the map internally or an outside firm is engaged, if the assumptions incorporated into the plan are not realistic, it will be a road map to disaster rather than a useful tool to guide the company through a difficult period.

The most important and often elusive ingredient affecting the development of projections is always the company‰¥ús level of sales activity. Sales activity projections must be developed through meetings with sales and marketing managers, who are then responsible for supporting those projections.

If the projections are prepared properly on a conservative basis, areas of expense expressed as a percentage of those sales levels measured by the company‰¥ús previous and present operating experience will be more meaningful, resulting in a more accurate set of projections. Working capital requirements can then be backed into, and a firm operating budget on a monthly basis of both profit and loss and cash flow will emerge as an extremely useful tool for the company‰¥ús future planning.

If midway through the year, substantial unprojected orders are received that dramatically alter the company‰¥ús map, a new set of projections must be constructed. The company cannot operate over the next several months using a road map that was developed on information that no longer represents the actual circumstances.

Encountering serious financial problems is a crisis in the business cycle that requires immediate action to avert collapse. Operating budgets are effective tools to make managers financially responsible, provided they are developed accurately and do not serve as a convenience for principals.

In preparing for an economic slowdown, owners and CEOs must be disciplined and experience the pain of problem-solving and get it over with by taking the time to solve the problem. They must accept responsibility for the dilemma and deal with the issues honestly.