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BUSINESS GUIDE

7 Secrets of Recession-Wise CFOs

How Top Finance Leaders Engineer Resilience Into Their Operations

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How Top Finance Leaders Engineer Resilience Into Their Operations

Can a hawkish Federal Reserve pull off a soft landing for the economy while putting a lid on inflation? Maybe, maybe not. But CFOs in leading firms aren't banking on anything. They're taking steps to keep their companies on an even keel no matter where the economy goes.

Not that a soft landing is impossible: A better-than-expected gross domestic product report, which showed GDP up by an annualized rate of 2.9%, combined with slowing inflation and avoidance of a rail strike that could have resnarled supply chains are causes for optimism.

Still, recession-wise finance leaders are sticking with their plan to hope for the best and prepare for the worst.

This business guide offers seven practices of CFOs who focus on insulating their companies from economic fluctuations, year in and year out. Even if a downturn never materializes, these measures will make your business more resilient and ready for nearly any circumstance.

7 Secrets of Recession-Wise CFOs

First, there's one thing top finance leaders don't do, and that's sit by passively until they're forced to slash spending and schedule layoffs. Start now with these seven steps, and set your company up to weather whatever may come next.

1. Constantly assess cash flow and employ rolling forecasts.

Preparing for either a downturn or a sudden upswing or market opportunity starts with a cash flow analysis to assess your working capital and continues with establishing rolling forecasts that will help you dynamically adapt to market and economic changes.

In addition to the standard cash flow statement, resilient CFOs keep a particularly close eye on their companies' free cash flow or the money left from revenue after subtracting operating expenses and capital expenditures. That gives leaders a clearer view of the cash available for financial reserves, expansion investments, or discretionary spending.

Once you have a handle on cash, implement a rolling forecast methodology that allows you to continuously update your assumptions.

The defined period you use for your forecast should vary based on conditions. Common options include forecasting for the next 12, 18, or 24 months. When a recession is possible, shorter is better to reliably project outcomes — your focus is on getting accurate cash flow projections for the next quarter or two.

Smart CFOs also:

- Keep an eagle eye on their cash on hand. The longest recession since World War II was 18 months, so when a downturn is on the horizon, the goal is to have enough capital reserves to make up the difference between various levels of reduced earnings and the income needed to maintain operations for that length of time, as we'll discuss.

- Know their liquidity options. Businesses that line up capital sources before they need to access funding are better positioned to get favorable terms. Sources may include revolving loans and other credit lines, owner infusions, alternative financing, private equity, and government resources such as SBA loans.

- Bake customer and supplier health into the cash calculation. Top CFOs use technology, including a data warehouse, to keep their fingers on the pulse of key customers and suppliers. Begin quarterly business analyses of all, or at least your largest, customers. Identify where you may need to enforce contracts to control your exposure and which clients might be slow or unable to pay. Consider adjusting terms or throttling lines of credit where appropriate. Some companies use downturns as an impetus to "fire" unprofitable customers.

Negotiating payment plans with suppliers while offering incentives to customers for early payments or bulk orders not only improves cash flow but may create goodwill that lingers.

More on customer and supplier health in a bit.

2. Maintain tiered forecasts with proactive yet surgical cuts.

CFOs who don't stress excessively about downturns have in their back pockets a variety of spending plans aligned with likely economic conditions and their own cash flow realities.

One approach is as simple as compiling tiered forecasts representing cuts to respond to revenue reductions of 10%, 20%, and 30%. All line items are on the table, and plans include enough specificity that the CFO is confident the company can achieve expected savings if needed.

Reductions are Response 101 if a downturn materializes, and now you have percentages to aim for. But go too far, and you'll leave the company at a disadvantage. Aim for cuts that you can dial back as conditions improve. Layoffs, for instance, are not easily reversed, particularly given persistently low unemployment.

For some historical perspective, leaders who weathered the 2008 recession may recall a report called
"Roaring Out of Recession" that Harvard Business Review released in 2010. It looked at data from 4,700 public companies during the three years before the recession, the three years after, and the recession years themselves.

HBR researchers found that 17% of those companies went bankrupt, were acquired, or became private. The majority had not yet regained their pre-recession growth rates three years after the official end of the downturn. Only about 9% prospered after the slowdown, defined as outperforming both their own previous performance and that of their rivals by at least 10% in terms of sales and profit growth.
What did those leaders do right?

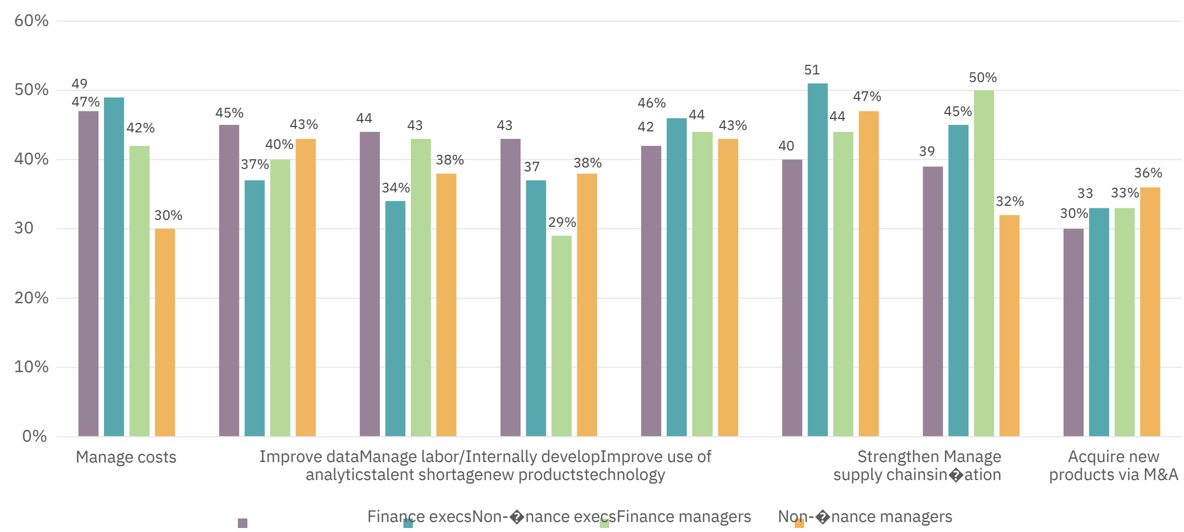
Turns out, massive cost reductions don't predict success. In fact, companies that made deep cuts had the lowest probability, 21%, of pulling ahead of the competition when times got better.

Increases aren't the answer either; businesses that invested more than their rivals during the recession had only a slightly better, 26%, chance of becoming leaders after a downturn.

The key is determining which cuts to make, when. In their book *Cut Costs, Grow Stronger*, Shumeet Banerji, Paul Leinwand, and Cesare Mainardi address the idea of reducing costs without negatively impacting performance through a concept called "capabilities-driven cost reduction." In this framework, CFOs identify their companies' key capabilities, defined by the authors as "the interconnected people, knowledge, systems, tools and processes that establish a company's right to win in a given industry or business."

Your business's capabilities are strengths, usually around two to five, that provide a clear advantage in reaching and serving the customers you care about most.

Besides Improved Revenue and Profit, Choose Top Priorities Over the Next 18 Months



Data: NetSuite Spring 2022 Survey (500 respondents)

Then, they rate activities to ensure spending nurtures these capabilities. This rating process is typically based on three questions:

1. What do I need to keep the lights on? For example, sales and general and administrative expenses.
2. Where am I spending that will make a difference over time in terms of winning in our market?
3. How do I keep the rest as lean as possible?

Once you've identified what matters, consider using a modified version of zero-based budgeting, where expenses are justified one by one and budget owners must show how spending is aligned with identified key capabilities.

Zero-based budgeting had a mini popularity boom during the pandemic, as CFOs looked for strategic, targeted savings opportunities. It can be time- and labor-intensive, but finance leaders find it's often worth the effort when their companies have many fixed costs, duplicative spending across the organization, or budget silos that limit visibility.

T&E spending is generally the first area to see deep cuts. Outsourcing certain high-cost functions may also be an option, as is slowing or stopping speculative projects until the economy picks back up. One quick way to get staff to rethink their habits: Require executive approval for most discretionary spending. There's nothing like justifying expenses to the CEO to make requesters assess the criticality of any outlay. New controls, policies, approval workflows, more visibility through better software — all can help keep a lid on spending.

Employee layoffs, real estate consolidation, and other asset sales, along with eliminating product or service offerings, are more drastic efforts that CFOs know will be difficult to roll back.

Here are examples of tiered scenarios with associated responses:

Scenario 1: A short recession and quick bounce-back.

In this scenario, the recession lasts about six months. If your company has less than six months of cash and debt capacity, operating expenses should be reduced on the order of 5%, with a particular focus on reining in variable, nonessential costs such as travel.

Extend payment terms with vendors to the extent possible. Delay hires not absolutely critical to the functioning of the business. Headcount reductions are likely not necessary now, though salary reductions may be instituted for a temporary, pre-set period to extend your runway. Make the cuts needed to extend your cash runway beyond six months, minimum.

Scenario 2: A six- to eight-month recession and gradual recovery. In this scenario, resembling a swoosh-shaped recovery, the recession lasts six months or slightly more but the economy takes longer to bounce back. If your total projected revenue, cash, and debt capacity does not exceed nine months, then beyond the moves recommended in Scenario 1, map out headcount reductions and steeper cuts in operating expenses, in the 10% to 15% range. Pencil in the moves needed to take your cash burn to nine months.

Scenario 3: Lowered revenue extends past eight months, and recovery is sluggish. In this scenario, business drops then flatlines for six months or more. Operating expenses must be reduced beyond the relatively modest cuts in the two scenarios above, on the magnitude of 20% to 25%. Plan further headcount and other reductions to preserve a cash runway of at least nine months, ideally 12.

3. Embrace customer segment analysis exercises.

While no company is completely immune to a downturn, many industries and business models are recession-resistant, meaning they fare well even when other companies are slashing costs and struggling to survive. The most recession-wise CFOs know this and take lessons from these firms.

Consider how customer demand and supply availability might change if the economy slows. Are you certain of your products extravagances versus necessities? Modeling likely buyer behavior will provide insights into how you might adjust production.

On an individual level, customer analysis is critical. Look at how client businesses weathered the pandemic, how many are at risk, and at what level and what percentage of your revenue comes from those that might not survive an extended downturn.

8 Dos and Don’ts of Cost Cutting

Do	Don’t
Address operational inefficiencies by identifying redundant positions or processes that can be eliminated or restructured.	Cut strong talent. Smart, committed employees are hard to find and even harder to retain.
Consider cutting initiatives that are not core functions of your business and products or services that are underperforming. Profitability comes to the front of the queue, even for growth-oriented firms.	Cut marketing too deeply. Consider social and other inexpensive brand-awareness drivers popular with startups. Customers and potential customers shouldn’t be allowed to forget about you.
Consider taking payments off autopilot to better control timing, and thus cash flow and discounts. Cancel underutilized subscriptions.	Cut technology that helps your team work efficiently. Automation is a lifesaver when headcount reductions are needed.
Be transparent with employees if pay or benefits need to be frozen or temporarily cut. Consider scaling back salaries or hours worked while keeping benefits intact.	Cut areas generating positive cash flow. And be judicious with cuts to sales, SEO, or digital ad spend.

Your ERP can generate data to gauge the financial health of customers. Consider running per-client business reviews of metrics including current accounts receivable, return on sales (ROS)/operating margin, and sales growth rates to spot changes in buying patterns that could indicate a decrease — or an increase — in demand for the customer's products or services.

Also mine this data to see which clients might benefit from proactive outreach, whether to head off slow payments or upsell those that could benefit from more of your product or service.

Can you adjust the rates on some service offerings to keep cost-conscious buyers from canceling?

Examples of enticements include product bundling and unbundling, installment plans, and the ability to add or remove features. In recessionary times, value sells. How might you give the customer more while still meeting margin goals?

4. Evaluate the supply chain on a set, regular basis.

When recessions hit, customers may stop buying, while suppliers cancel orders and delay deliveries. Recession-wise CFOs know that the last thing they want is to be left with idle production lines and some orders they can't fulfill even as other inventory piles up.

That's why these CFOs closely monitor upstream and downstream supply chain risks. Here's how:

1. Run a supply chain mapping exercise. Build a map or flowchart of all suppliers, no matter how small. Keep the map updated as you add new partners and stop working with others. Use it to flag duplicate and single-source suppliers. Then, go a step deeper and evaluate suppliers to your most important suppliers. If you purchase components that include semiconductors, for example, where is the supplier getting its chips?

Learn More

Cash Flow Analysis: Basics, Benefits and How to Do It. Cash on hand determines a company's runway — the more cash on hand and the lower the cash burn rate, the more room a business has to maneuver.

Zero-Based Budgeting Revisited: A Practical Guide. ZBB is a budgeting process that starts with a completely blank slate. Fans say it's helpful. Critics say it's unrealistic. We identify common pitfalls and detail how to avoid them.

9 Ways CFOs Can Maximize Liquidity Now. By understanding your current liquidity profile and forecasting future needs, you can preserve cash in the short term while positioning your company for growth.

How 5 Businesses Use NetSuite Analytics Warehouse for Deeper Data Insights. Since the debut of NetSuite Analytics Warehouse, companies across industries have produced impressive results with the solution. They've slashed infrastructure costs, fine-tuned forecasting, whittled product lines, and monitored the metrics essential to expansion.

In some ERP systems, all information related to each supplier is located within a central vendor management record, so decision-makers can easily keep track of relationships and inform supply chain mapping efforts. Look for a vendor scorecard function to track supplier performance — and keep in mind that it won't deliver insights without at least a couple of years' worth of data.

2. Apply a weighted ranking. Devise a list of risk factors, like disruptions, financial dependence, credit history, or susceptibility to recessionary pressure. Give each of those factors a weighted importance and each supplier a score of 1-5 for each, with 5 representing the highest risk. Then, calculate the weighted average of those numbers to come up with a score that represents a supplier's total risk. Consider the criticality of high-risk suppliers to your business.

3. Identify areas for diversification. Once you understand the risk attached to each supply chain partner, rate the areas where you need to add diversity by, for example, finding redundant sources for key parts and materials. One silver lining of a recession: You may find suppliers that were once overbooked will welcome your business.

4. Take deeper advantage of your vendor management software. If your ERP offers a central record of all information related to each vendor, mine it to see if favored suppliers could provide components or materials that you currently purchase from a one-off supplier, thereby providing an opportunity to drive down costs and complexity.

One side benefit of this customer and supplier analysis? An improved ability to renegotiate contracts.

Meanwhile, recession-wise finance leaders know that while many companies strengthened their supply chains over the past few years, a recession introduces new variables, like customers potentially opting for the lowest cost over speed of delivery or higher quality. In response, CFOs may want to advocate for a shift in focus, favoring value pricing or supplier financial health over the ability to deliver materials quickly.

Oh, and all those years spent making the supply chain as lean as possible? Much of that has been rethought in the name of resilience. Losing a sole-source or major component supplier or one that offers a custom-made part can seriously disrupt production — just when you need cash flowing.

Consider spending to increase supply chain flexibility, even going so far as to acquire suppliers, particularly if they're struggling. That's the sort of out-of-the-box thinking that distinguishes top CFOs.

More Resources

- **Recession-Proof Defined.** When a recession hits, many companies face the prospect of declining revenues and profits. But some businesses perform well even when economic times are tough.
- **What Is Revenue Leakage?** Companies don't always do as good a job collecting revenue as they do selling their products and services. Unearned discounts, billing mistakes, and penalties that get waived mean a dollar's worth of sales doesn't always end up as a dollar's worth of revenue.

Smaller organizations without the buying power of their larger competitors may instead evaluate partnerships with an eye to increasing their clout. That trend is called collaborative planning, forecasting, and replenishment, and it involves close coordination of purchasing, both among departments and with external partners.

Collaboration can also help your company establish stronger relationships with existing suppliers. Increased purchasing volume protects against supply chain disruptions and could make you a favored customer. Barring that, longer contracts and a willingness to be flexible can potentially win you better terms and preference when stock is low.

CFOs with a deep understanding of their companies' contracts are in a strong position. Review contracts for enforceability and other potential risks, such as dispute resolution, early termination, or price review mechanisms and adjustable service-level agreements.

CFOs should also keep tabs on the term flexibility that their sales teams are empowered to offer clients. Any favorable payment provisions you extend will likely be stretched out during a recession, and that can prove costly. Again, requiring executive approval on special terms will incentivize sales to limit use of discounts and other incentives.

However, it does make sense to offer rewards in return for contracted sales volume. Businesses should also evaluate if they can provide inexpensive value-adds or added flexibility in exchange for faster payments. In addition to enhancing variables that help stabilize revenue streams, being flexible can create goodwill and repeat customers.

5. Get involved in inventory management strategies.

Hanging on to excess inventory is never a good idea. It can be even more costly during a recession because slowed demand may make goods more susceptible to obsolescence and increase storage and carrying costs.

On the other hand, some extra inventory is a buffer against supply chain issues.

CFOs understand that, from a financial standpoint, inventory has an impact on cash flow. Information about the location of products, their turnover rates, and exact status — on order, in transit, allocated to an existing customer — is tied to reorder dates, and thus to predicting future cash needs. When will the procurement team need money, and how much?

Thus, demand planning is important. Slowdowns may be uneven across product lines.

If your plan includes decreasing the use of incentives and specials, for example, it's time to focus on core offerings while watching inventory turnover.

Demand planning starts by identifying less popular, less profitable items. If necessary, here's where you begin reducing production and inventory, turning to sales or volume discounters to get that stock out of your warehouse and off your books. Have systems and processes in place to zero in on the minimum inventory you need to reliably accommodate predicted swings in customer demand or supplier delays/outages.

Recession-aware CFOs understand how inventory impacts their companies' cash flow and profitability.

The supply chain disruptions and rising prices and demand we've seen over the past year likely made your ops team hyper-focused on having enough stock to meet demand, with less emphasis on tight cash management. How might that calculation change in a recession? For one, financial management needs to be more prominent in your inventory management and material requirements planning strategies.

Three areas to assess:

1. Ordering too much stock when demand is cooling increases carrying costs and ties up in inventory cash that you may need elsewhere. Stay on top of demand planning.
2. Adjust your economic order quantity (EOQ) formula to recalculate all fixed orders that are triggered when stock reaches a predetermined minimum.

$$\textbf{EOQ} = \sqrt{2DS / H}$$

Where: D = Demand in units per year
S = Per-purchase order cost
H = Holding cost per unit, per year

3. Other inventory planning metrics you can track using your ERP include carrying costs, daily sales or movement of inventory, and forecast and system accuracy to quantify how precisely your system reflects physical stock.

6. Use automation to refocus workers on higher-value tasks.

The job market is incredibly tight, and salaries are still on the rise. Even if a recession eases the talent squeeze and brings labor costs down, or at least levels them off, payroll remains the biggest expense on a typical company's balance sheet.

Given these realities, it's less expensive to upskill existing staff than to find and onboard new workers, even at a lower payscale — and especially if you need to train them.

Recession-aware CFOs don't delay in investing in technology that can automate manual tasks and, in the process, free up headcount for that upskilling and more strategic work. Whether in the warehouse, finance department, or customer self-service, automation can negate the need to fill some empty positions while providing a path for existing workers to gain new skills.

Automation also gives businesses breathing room to reevaluate workflows, fine-tune processes, and implement new technology. Advanced systems provide real-time data and reporting dashboards, including KPIs, enabling leaders to closely monitor results and react quickly.
In fact, automation closes the loop on monitoring cash flow, and it helps eliminate manual AR and AP tasks, speeding up the process while also reducing the number of errors. Automating manual accounting tasks delivers increased efficiency and better data quality, lowers labor costs, and mitigates risks including invoice fraud.

Where to start? Find three or five rote, slow, error-prone, human-based processes that suck the life out of staffers and leave decision-makers with incomplete or suspect data. For accounting, that might include things like three-way matching, invoice creation, and sending customer payment reminders. Zero in on these repetitive manual tasks one by one, and figure out how you can automate them. Doing this now will set the business up for success as the economy resets itself for growth.

Learn More

Reorder Point Defined: Formula & How to Use. A simple, rules-based approach to reordering saves time and reduces the possibility of costly mistakes in inventory management.

What Is Zero Inventory and Why Is It Important? While inventory represents an asset, it's an asset that

can
decrease in value, costs money to store and maintain — and ties up cash.

3 Ways to Score Automation Wins

Top areas where every company can improve are finance, marketing, and HR.

Finance

Automation saves considerable time on accounts receivable (AR) and accounts payable (AP) as well as other financial processes managed on a daily or weekly basis.

Marketing

Start small by using software to build and blast monthly emails with content or offers to a client distribution list, then move up to granularly segmenting your customer database and micro-targeting groups with personalized messages.

HR

A human resources management system automates onboarding, time off, benefits, and payroll and tracks the employee lifecycle to provide insights into workforce productivity and efficiency.

7. Harness technology for scenario, cash flow, and other planning.

When growth slows, leaders scramble to get a holistic view of the business to make sure it's operating as efficiently as possible.

Recession-aware CFOs don't need to scramble because they regularly use insights gained in the previous steps to game out potential scenarios by modeling elements such as new sales, upselling, and cross-selling to existing customers and business renewals on a monthly or quarterly basis.

As an example, compare freezing hiring for six months or a year versus building a workforce that can aggressively expand sales and take market share from your competition. What gets you the biggest win?

Top scenario planners use a three-step process to find out, aided by technology like ERP and financial software:

1. Identify critical triggers even in the midst of uncertainty. When faced with a crisis, finance leaders quickly establish salient facts, like cash position, and develop guidelines for how the organization should respond. Scenarios are built on a set of assumptions around events that affect the survival of the organization and should trigger a series of actions.

NetSuite helps with:

- Optimizing cash flow. NetSuite Financial Management provides real-time access to bank and credit card data, accelerates the reconciliation process, boosts the accounting team's efficiency, and, importantly, provides an accurate picture of your current cash position.
- Planning and budgeting. By automating labor-intensive planning and budgeting processes with NetSuite Planning and Budgeting, finance teams can quickly and easily generate forecasts, model what-if scenarios, and provide up-to-date reports.
- Data analytics and BI. NetSuite Analytics Warehouse is a cloud-based data storage and analytics solution that consolidates data from NetSuite and many other business applications to deliver powerful data analysis that drives actionable insights. Business professionals can load data and easily build and run their own analyses without relying on IT.

- Automating cost controls. Purchase management with NetSuite Procurement helps ensure you buy goods and services at the best price and the right time by channeling purchase orders to approved suppliers with pre-negotiated contracts.

2. Develop multiple scenarios, but keep it simple. It's easy for finance teams to feel overwhelmed by the range of potential outcomes. That's why it's best to focus on two to three major uncertainties, like headcount needs versus salary and benefits costs or accounts receivable risk, and build scenarios from there.

NetSuite helps with:

- Projecting workforce costs. By using workforce planning functionality in NetSuite Planning and Budgeting, companies can create recession-adjusted hiring plans by modeling future workforce needs using actual payroll, expense, and headcount information.
- Keeping tabs on customer health. Identifying at-risk accounts before they miss payments or cancel orders enables you to reach out and arrange payment plans while adjusting credit appropriately. NetSuite CRM provides an in-depth view of each customer.

3. Build a nimble response strategy. Each scenario should contain enough detail to assess the likelihood of success or failure of different strategic options. Once this is all in place, finance leaders can create a framework that helps the executive team make decisions, then track results in real time so the company can be nimble in its ongoing response.

NetSuite helps with:

- Monitoring KPIs. Scenario planning ensures you're tracking the right metrics for now. Then look to SuiteAnalytics for real-time visibility into operational and financial performance across all business functions.
- Improving inventory and order management. NetSuite Inventory Management provides a single, real-time view of inventory across all locations and sales channels to respond to changing sales patterns, while intelligent order management and fulfillment decrease the cost of goods sold.

The Bottom Line

There's a saying that recession-wise CFOs live by: "Fix the roof when the sun is shining."

Slowing growth creates an incentive to reevaluate business processes, but ideally, planning and improvements begin when times are good. When growth is slowing, your people must work harder to make each sale. Restructuring when everyone is paddling as hard as they can is painful. So start working now to ensure your business is ready to ride out any potential storm.

More Resources

- **Stagflation vs. Recession: What's the Difference?** While recessions are relatively common, stagflation is much rarer — yet potentially even more damaging. Here's how to understand the differences.
- **What is a Financial Contingency Plan? A Step-by-Step Guide to Creating One.** Creating a financial contingency plan is a wise move for any business because crises and setbacks can strike suddenly. Contingency planning lays out, in advance, how to respond to scenarios and get the business back on track.
- **A 6+6 Budget Might Not Make You Popular, But It Could Save the Business.** Asking people to rebudget is not a move to be made lightly. That's especially true when rebudgeting downward. Still, when your plan is useless, you have to rework it.

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