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SURVIVE THE RECESSION

How the Current Economic Crisis Might Impact Staffing

Once upon a time the stock market was considered safe, and everyone lived happily ever after. But the market is just a reflection of the economy, which will impact employment and staffing, so we need to understand what is happening here. The market is built on confidence, which is a very frail thing, and there have been financial panics every 20 years or so starting in 1819, some of them severe. We are currently in a two-stage decline – the first caused by the credit crisis due to the subprime housing meltdown and, after brief recovery, the second drop resulting from a fall in corporate profits with 500-1,000 point swings in the Dow commonplace. No one really knows where the bottom is.

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A totally free market system is over with the government securing equity positions in corporations, and foreign countries taking coordinated actions to shore up an integrated financial and banking system. We will not know for many months the impact these actions will have but hope that the economy bottoms out by mid-2009 with unemployment cresting a bit over 8% by year end, although this can vary from state to state, followed by a slow improvement. Our latest unemployment rate is 6.5%, the highest in 14 years, but we are dealing with uncertainty on many levels. The new Congress, President and world leaders will have their work cut out for them.

navigate through this period, and some companies will prosper as they take advantage of unfolding opportunities.

THE GENESIS OF THE CRISIS

We now know that the government and financial excesses made a mess of things, and the alarm bell was not sounded early enough. Even icons like Allan Greenspan admitted that they were asleep at the switch. We are cautiously optimistic about an imperfect bailout plan. We now know it will cost much more than the original $700 billion rescue plan; every day brings another surprise. There is no free lunch. We are in a lot better shape

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Corporate profits are up in some low-end businesses such as McDonald's and for top-of-the-line companies such as Apple, but a general recession is taking hold, with most companies showing declining profits and laying off staff. Wachovia (before the Wells Fargo merger) lost $24 billion in the last quarter and China has shut down 50% of its toy factories. This is just a small sampling of the bad news. Oil, which was selling for $147/barrel and is projected to rise to $200, is off more than 50%, reflecting lower demand, but which is good news for inflation.

We go through a staffing shakeout about every 10 years. The last one was the dot.com bust, impacting IT the most. Well-managed companies will make it through with discipline and effort, but not all will survive. Those that come out the other side will have less competition, higher margins and should see about seven good years before the next inevitable tsunami from some yet unforeseen event. We suggest that by implementing the prescripts discussed in the last section you can

than most other countries. They still put their reserves into the dollar, and the Presidential election results make other countries feel more secure. Other nations with far lower GDPs are putting relatively more money into their own bailout packages than we are, with less of an infrastructure to manage them.

The problem started, as it often does, with good intentions, followed by unintended consequences. The idea was to help people who could not qualify for conventional financing with low adjustable rate mortgages (ARMS) to get into the housing market. The problem was that paying higher rates became impossible, as homeowners were squeezed by $4-5/gallon gasoline, galloping inflation and flipping homes in a speculative housing market. When a balloon payment came due the housing bubble burst, and defaults cascaded into toxic mortgages. But the homeowners had no equity in their homes so they could just walk away when they ran into trouble. The lenders were already bundling mortgages to third parties sold as high-grade mortgage-collateralized securities sold by names like Goldman Sachs, Bear Stearns, Lehman Brothers and numerous hedge funds, mostly rated as Triple A paper by S&P. Who would not invest?

Long gone were green eyeshade types applying old-fashioned GAAP and FASB accounting rules. Then some really bright PhDs in math and physics transformed mundane mortgages into a magical and exotic new class of financial instruments called derivatives. These were highly leveraged investments with good yields, driven by naked shorts, market-to-market accounting and created a mind-boggling $600 trillion market along with $62 trillion in credit-deferred swaps.

The problem was there was no transparency in this unregulated betting parlor with minimal assets behind them with just $167 trillion of worldwide assets on a $63 trillion GDP. It just didn't add up and was like the Enron fiasco on steroids. This contaminated the worldwide financial system and resulted in the first phase of the crash referred to above. The proverbial house of cards fell when Lehman went belly up. So the Paulsen, Bernanke brigade came in, and the full magnitude of the crisis unfolded overnight and the whole world is still fine-tuning a solution. But as goes confidence, so goes the stock market, profits, layoffs and unemployment.

THE STAFFING SOLUTION

So where does this all leave staffing? The simple answer is that it is too early to tell the full magnitude of the problem, but unemployment will rise and hiring will slow down in 2009. The good news is that there are ways to get through a recession and capitalize on opportunities. So here's our top 10 list of things to do.

1. PLANNING. Since no one really knows what will happen in 2009, it is only prudent to hedge your bets more so now than ever before. The best way to do this is to develop a proactive game plan, which includes creating alternative scenarios to deal with various unknowns. You need to be able to think through the ramifications of changes before they happen wherever possible to avoid surprises and to evaluate different courses of action while you have the luxury of time. We suggest developing both strategic and tactical business plans. Strategic planning means dealing with big picture issues such as identifying which economic sectors and industries are likely to be least impacted by the coming downturn, how you can partake in those staffing sectors serving those industries, what geographic areas are the most recession proof, etc. Tactical planning includes dealing with such factors as who will be responsible for identifying and penetrating the sectors and specific accounts that have been targeted, how much money you will need to enter those markets, when you will need to secure those funds, how you will reorganize your operations to implement these tactics, etc. Make sure to involve all those people, internal and external, to your organization that you need to make informed decisions, backed up by current data and not suppositions.

2. CLIENT, CUSTOMER AND CANDIDATE RELATIONS. Your survival depends on being profitable, and everything starts with sales. So we have broken out revenue into four groups:

- **Key Clients**, where you have a strong relationship and do a lot of business
- **Other Clients**, where strong relations exist, but where you do limited volume
- **Key Customers**, where sales are good, but it's all about price and you are just another vendor
- **Other Customers**, where sales are low and you are just another vendor

If there was ever a time to get close to the above groups it is now. Your priority should be to lock in your Key Clients, then maximize your volume with your Other Clients, then find out what is needed to convert your Key Customers into Key Clients and lastly to increase your business with your Other Customers – as long as in all cases these actions make economic sense. Remember that while you are doing this your competitors are likely doing everything they can to woo them away from you, and a good defense is the best offense. Get to know their key decision makers and their hot buttons. Find out what they are thinking by spending quality time with them in an informal setting to lower communications barriers. Find out how you can help them. Here is a sample of some of the questions you might ask and issues you might address:

A. Are they planning to grow or downsize? If so, in which areas specifically and when?

B. Find out how you are doing and how you can better meet their needs. If they are dissatisfied with some aspect of your services, find out why. Do some fence mending before they go elsewhere.

C. Come up with win-win solutions even if it costs you some money in the short run.

D. Are they being solicited by your competition? If that is the case, is there something that they will deliver that you are not providing? Determine the seriousness of the threat, and either be able to dismiss this as a concern or determine what is needed to retain their business.

E. Help them uncover problems before they do, and become a trusted resource that they can rely on to help them weather the downturn.

This brings us to our temp and perm candidates. We obviously can't make placements without them so your recruiters need to treat them with care and respect as jobs become scarce and nerves become frayed during the downturn. Provide them with honest career guidance as in today's blogosphere world you can't afford to have your reputation trashed by treating people poorly.

3. NEW ACCOUNT PENETRATION. While you are defending your flanks you need to proactively pursue new business to make up for the inevitable losses of clients and customers due to the laws of probability. As we would defend our client base we need to create a game plan to take accounts away from our competitors, who will jealously be defending their customer base in a down economy. You will therefore need to be that much sharper to penetrate new accounts this year. There are several main elements to successfully implementing such a program.

These include:

A. Assess your marketplace to determine where the opportunities lie in terms of volume, margins and growth, for the short and longer term.

B. Determine the major users of the people you place or areas you can reasonably expect to expand into.

C. Find out who your main competitors are and how you stack up. Make a realistic assessment of your ability to penetrate those accounts. In some instances it may not be possible or worth the effort in terms of time or profit potential.

D. Honestly assess your relative strengths and weaknesses and address them. For example, you may need to increase your line of credit to finance receivables, you may not have the personnel needed to serve a more sophisticated clientele, you may need to add staff to handle more business, etc.

E. Create a top 10 list of target accounts (or whatever number seems appropriate to your market) for each of your sales reps so that they have specific targets to penetrate.

F. Develop a game plan for each new account. Assign individual responsibilities to first land the account and then service it, set financial targets, monitor your progress and modify the plan as needed.

G. Create the tools to do battle:

- Start a competitive price list, including what will be your bottom line.
- Establish a cold call list to find prospects; there are many commercially available sources.
- Make sure you have appropriate collateral materials to represent your capabilities properly.
- Create a family of value-added services to separate yourself from the competition so that getting business is not all about price; i.e., testing, skill assessment, salary surveys, cost-savings programs, consulting, alternative billing methods, performance guarantees, project solutions, etc.

4. METRICS. In order to know if you are on the right course you will need to create and monitor your metrics and build a sound game plan. A qualitative assessment is important such as: do you have confidence in the people that you have put in charge of your program, and do you have the time, energy and personal commitment required to make the plan successful? Beyond that you need to create and monitor the metrics that clearly tell you if you are making the progress that you intended. In a dynamic environment, you really need to have a finger on the pulse of your business to either reinforce what you are doing or make changes sooner rather than later. An example of external metrics would include an estimate of the staffing submarket you are in or are entering; i.e., the number of RNs in San Francisco County, their wage ranges, markups, projected growth rate, number of competitors, market share, etc. Internal metrics would include (again by submarket) things like telemarketing calls, assignments received per telerecruiting call, send outs per candidate, placements per job offer, duration of assignment, margin and bill rates, etc. We strongly encourage weekly tracking of these values to determine trends and set standards to have a yardstick for comparisons.

5. RESTRUCTURING AND COST REDUCTION. Doing business in 2009 might require that you restructure your operations to deal with the changing economic conditions. But restructuring is not the same as cost reduction. It is more complicated and includes concepts such as combining jobs or changing areas of responsibility. Cost reduction may be a necessity for many companies in 2009. Depending on your situation you may need to institute a 10% across-the-board cut in headcount or base salary. At a 20% margin rate every dollar you save is worth $5 in lost sales. You might restructure your comp plan with a richer incentive rate for incremental volume, so that the staff can more than make up for any lost base salary. Anyone can chop costs but it takes a good businessperson to make intelligent spending decisions. The key is to determine the cost/benefit ratio of your options. For example, you might redistribute your recruiting budget based on which sources generate candidates that you actually place (i.e., referral bonuses vs. job fairs and job boards). This may be a better decision than cutting recruiting costs across the board. You can run a small-scale test before fully implementing a program. What works in one area might not work in another. You must be able to separate your profitable lines of business from those that are not working well, but make sure to do this on a contribution basis before shared costs. Once you have made your decision implement it without delay and concentrate your efforts on what makes you money. However, consider the implications on the morale of the team, and that you will be coming out of this downturn eventually and will need to retain your top people over the long haul.

"I am often surprised how few staffing companies have instituted sound credit policies."

6. CREDIT AND COLLECTIONS. I am often surprised how few staffing companies have instituted sound credit policies. The average staffing company does a good job in collections, but grants credit too easily in the first place. Back in 2001 we saw staffing companies go bust due to huge write-offs to companies they never should have granted credit to in the first place. This is bad enough in the perm sector, but in temp and contracting it can be a disaster. Assuming Client A was not a good credit risk and was using temps at a $40-per-hour pay rate and a 15% burden rate, each month a temp is on assignment, there would be an $8K/month outlay. If that client had 25 of your employees on assignment this means you are paying out $200K a month. Based on 100 people on assignment at this pay rate and a 40% markup, your sales would be $11 million a year. Assuming a 4% pre-tax profit rate you would be generating a $460K annual profit. If Client A's payments were 8 weeks (60 days) that would translate to $448K in receivables. If it defaults, your profits for the entire year could be wiped out. If the credit limit was reduced to only two weeks due to the financial condition you could have reduced the write-offs by 75% or $336K. Therefore, you should consider tightening up your credit and collection policies immediately, and don't let write-offs sink your company. This is no time to play banker.

7. CASH MANAGEMENT. The bulk of the banking crisis appears to have passed and there is no need to put your money under the proverbial mattress, but you still need to manage your cash wisely. Although things look all right now, the new rules of the road have not been tested yet. The traditional recession with layoffs and business closures is far from reaching its full magnitude. So consider securing at least part of your line of credit as some companies have seen their LOC reduced. You can take down some of the funds that you need and invest the proceeds in secure short-term instruments even though there will be an interest rate penalty, or at least line up emergency funding such as interim factoring and nontraditional sources of capital. But watch out for the fine print. Make sure you have enough liquid reserves to cover your payroll for any contingencies that may arise, and invest only your excess funds to earn money. For example, there are still high-grade midterm principle-protected instruments out there that, when held to maturity, are sound investments. But putting your cash into the market today, even when investing in diversified mutual funds, is still risky.

Your objective should be to maximize your business profit, not to try to make money on your investment portfolio.

8. SOUND MANAGEMENT. The job of the CEO and management will become much more taxing in 2009 and will truly test their mettle. They will have to balance the need for capital conservation with the ability to create a vision for the company and build a game plan. They will need to identify opportunities and implement change where needed. The next step is to translate this vision into success by selling that vision to the staff and motivating them to getting it done. Obviously one must hire, train and retain good and loyal personnel. It is axiomatic that if you start with poor raw materials you can't build a solid product. You need to continuously upgrade the staff that you have and expand with quality additions. Sound management utilizes a combination of highly incentivized comp plans for sales reps and recruiters, individual and team recognition, meaningful perks, open communications, monitoring metrics, and creating a long-term retention plan for your key personnel, among other things. Strong leaders are self confident and build confidence in the people on their team. This will be more of a challenge in 2009 than in years past due to the uncertainties that we have already discussed. You can do the best with those things that are under your control. With respect to external events, react quickly and intelligently, and create contingency plans wherever possible. Lastly, a good leader creates an atmosphere of optimism and puts into perspective the constant stream of bad news that can be demoralizing.

9. STAFFING SEGMENTATION. There are very few sectors, geographic areas or companies that will be immune to the downturn, but there are ways to better position oneself for this period and to get through this cycle in relatively good shape if you plan ahead and implement the concepts discussed here. Nationwide, we are down 11% from our recent staffing highs. In the most recent issue of SI Report only seven major metropolitan areas (four of them in Texas) had job growth of at least 2% vs. last year. Two years ago the number was twice that. And just 21 smaller locales had job growth exceeding 2.5% (seven were in Texas, and four were in North Carolina). Two years ago this same number of locations had a minimum growth of 4.3%. Of 43 publicly traded staffing companies during the second quarter (the most recent period available), only 30% showed an increase in profits, which will surely decline in the subsequent quarters. Staffing Industry Analysts estimates that light industrial and office services temporaries, as well as direct hire, will show a negative growth rate this year, with most other sectors in the positive mid-single-digit range. During the last downturn only legal temp staffing kept its head above water during the entire recession. We believe that few if any staffing sectors overall will have a positive growth in 2009, but many companies can do quite well by thinking out of the box and implementing these and other steps. As of now healthcare, technology, defense and educational-related staffing sectors are holding their own. The government will likely spend half a trillion dollars on infrastructure projects in the next two years, and exports of capital goods to China are likely to be strong. But being in the right sectors is not enough. You still have to be on top of your game.

CREATIVITY. There is nothing like a crisis to create unique opportunities. So how can one prosper in a down economy? In the economy at large two of the fastest-growing subsectors, due to the explosion in foreclosures, are public storage, where people have to keep their furniture, or companies responsible for clearing out abandoned homes and preparing them for foreclosure sales (one third of all sales are expected to be foreclosures). Here are just a few staffing examples. There are many we could have extracted from our client base.

A. Move into a staffing subsector, which is recession proof if not even countercyclical, such as nursing, but where you have some experience. The dynamics of nursing is such that when a spouse is laid off nurses often find it necessary to go back to work in nursing, which is an area with high demand.

B. Consider emerging markets such as environmental or alternative energy sectors, which are relatively small but have strong growth prospects. Some of these specialties receive VC or federal funds, which can cover start-up losses and can support staffing fees when larger companies are cutting back.

C. If you are making a decent profit in your local market, have your management fundamentals under control and have financing available, you may have the opportunity to expand. You will need to find a good sales rep and manager for the new location market with the right dynamics and ideally have an anchor client in that new location. Make sure to set a realistic budget and monitor your metrics closely so that you can make mid-course corrections. If your assessments are wrong, cut your losses earlier rather than later.

D. Consider partnering with a complementary staffing company to reduce overhead and create synergy; i.e., partnering an L/I and engineering staffing operation servicing technical manufacturing companies. This will entail risks and necessitate structuring a sound legal agreement. Likewise, this may be the time to do an acquisition at what can be a bargain price in today's business climate.

Mike Neidle started Optimal Management in 1994 (www.optimal-mgt.com), 650-655-2190, mentoring staffing owners and managers to maximize sales, profits and company value. He was executive VP for Snelling and other staffing firms, as well as CEO, CFO, and marketing director, and in charge of econometric forecasting for startups to Fortune 500 Corporations. He has an MBA and a chemical engineering undergraduate degree.