

Don't Waste a Crisis: Emerge a Winner by Applying Lessons from the Last Recession

Competitive executives should welcome recessions. In the heat of a downturn, superior companies pull away from the competition and aspiring companies can dart ahead. In order to find patterns of success and failure, we studied more than 400 companies and their performance (relative and absolute) before, during, and after the last recession (1998–2004).

Our analysis yielded four types of firms: Stalwarts, strong firms that held their leads; Low Idlers, weak firms that remained weak; Disappointed Stars, firms that weakened; and Opportunists, firms that sped ahead during the downturn (see Figure 1). Four in 10 firms moved up or down within these categories during this time frame—a tremendous time for competitive change (see Figure 2). Those that emerged as Stalwarts or Opportunists created more than \$350 billion in market value, while the other companies destroyed over \$200 billion.

The key questions for any executive are:

- How did your firm fare during the last recession—were you a Stalwart or a Disappointed Star?
- How is your firm poised during this recession, both overall and compared to your competition?
- Did you learn the right lessons from the last recession?
- Are you performing the accurate analysis and taking the winning actions necessary to emerge stronger from this downturn?

Everyone Cuts Costs, but Only Some Benefit

All four quartiles cut capital expenditures as a percentage of sales, and all but the Disappointed Stars cut both R&D and advertising. However, only the top two quartiles (Stalwarts and Opportunists) increased gross margins during the recession year, and by the end of the recession had improved margins by 20%. In other words, they were smart about their cuts and successfully improved the design of their business (i.e., the configuration of people, assets, capital, and information to generate value for customers) to create operating

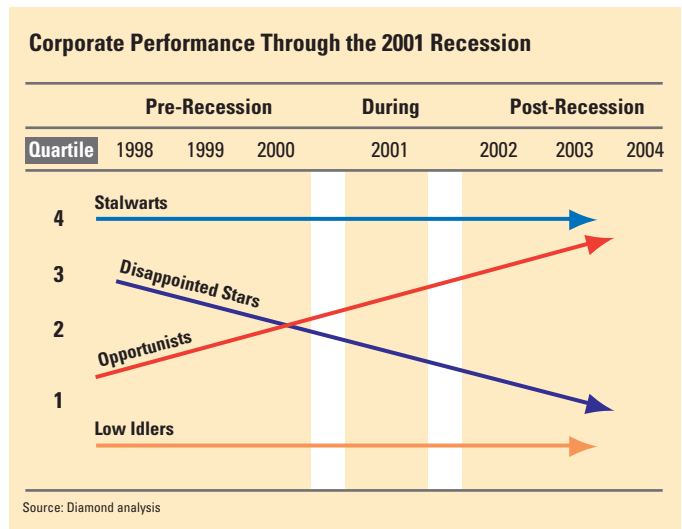


Figure 1

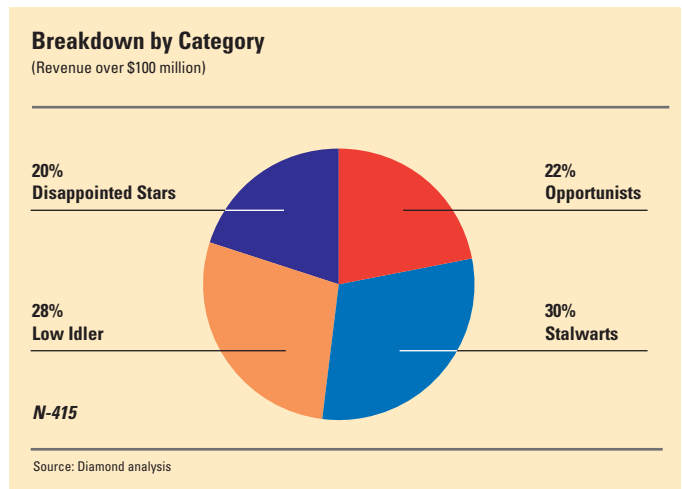


Figure 2

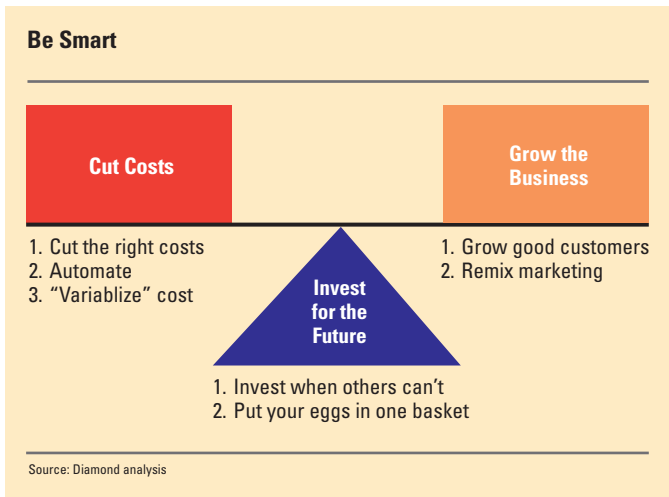


Figure 3

leverage that eluded others. The central lesson of our research is that at the very time when a leader is tempted to shorten his or her time horizon and make simple across-the-board cuts, superior performers dig into the data and act more intelligently than the competition.

Further analysis of the company recession data and of case studies revealed seven lessons to thrive in a downturn, while improving the fundamental design of your business (see Figure 3).

Seven Principles for Thriving in a Downturn

Principle 1:

Cut the Right Costs by Getting at the Root Cause of the Expense

Cutting costs across the board is generally a bad idea because money is better spent in some areas than others. Firms willing to perform a more thoughtful operations review—highlighting fixed versus variable cost drivers, in the context of the company's business model, servicing objectives, and organization—will yield much more value.

We helped a leading credit card company rethink its approach to service and were able to lower costs through customer self-service while increasing customer satisfaction. At a large insurance broker that was about to make an across-the-board cut of 10% on its technology budget, our analysis uncovered numerous opportunities for process standardization across the new business development group and identified more than 10% cost savings while simultaneously increasing their speed in setting up new businesses.

Principle 2:

Automate, Automate, Automate

Given the continued, rapid decrease in the cost of information technology, it is essential during a recession to search for new places to automate. Projects which may have been infeasible only a few years ago may now be economically viable.

For example, the Atlanta-based utility Southern Co. decided to invest in the installation of an automated meter-reading system in 2008. In addition to yielding cost savings from no longer sending staff out to read meters every month, the system will improve the company's business design by providing meaningful data around customer usage patterns, which will benefit both users and the company. In the future, Southern Co. could create an infrastructure to enable dynamic pricing.

Likewise, we worked closely with the management of a multi-billion dollar transportation company to architect and test the use of GPS and RFID technology on its vehicle fleet—dramatically lowering the cost for scheduling, routing, and maintenance, while improving driver safety and providing them with a platform for future innovations.

Principle 3:

Use Vendors to Drive Down Total Cost and 'Variablize' Your Cost

The meaning of "being a company" is more complicated today, so careful thought is required to determine which true core competencies to build in-house versus those that should be sourced from vendors or offshore providers. Companies that can optimize the resources inside and outside their walls hold the keys to maintaining and improving performance in a downturn and can use vendors to "variablize" their cost base. In some cases, companies can negotiate longer-term contracts to extend strategic relationships and reduce near-term costs. During the current economic downturn, the CIO of Johnson & Johnson pushed key software vendors for enterprise contracts in order to reap economies of scale. Now, all J&J entities receive benefits of volume pricing, which will save the company \$150 million a year.

Recently we helped a major investment bank create an on-demand, outsourced capability so they could flexibly ramp up and ramp down their IT staff to meet demand and their ability to spend—saving them millions of dollars in the process, while improving time to market.

Principle 4:

Identify Customers to Grow On

Rather than catering to all customers, unprofitable and highly transactional customer relationships should be re-assessed during a recession. Singapore Airlines recognized its best customers were business and first-class travelers flying transcontinental routes. Management cut back on short-haul routes, added long-haul routes, and invested \$300 million to improve business and first-class service. As a result, Singapore Airlines was profitable when East Asia fell into a recession following the currency crisis in 1997. It still remains more successful than other Asian airlines.

We also helped a large domestic airline redesign its channel strategy, inclusive of the Web, to change the nature of its relationships and interactions with key customers. In anticipation of the changing

nature of its customer base, our client is changing its approach to match the needs of its best customers.

**Principle 5:
Optimize the Marketing Mix**

Advertising and marketing spending are the first areas companies typically cut when faced with a down economy. Many of the leading companies today are busy looking across all their channels: Web, phone, direct mail, face-to-face, to match optimal channel to optimal interaction. In the process, they are taking advantage of new, more cost-effective methods of interaction, where possible.

For example, in financial services, there is tremendous interest in social media as a means to drive improved interaction with clients and increased trading. We are helping an investor services company, which has announced a new, comprehensive Web-based investor communications capability that allows brokerage firms to host their own investor chat rooms and validate how many shares of stock a person has in a given security, so investors can know if the person making the comments owns 10 or 10,000 shares of a given stock. Such social media hold the opportunity to drive customer interactions and transactions with minimal cost.

**Principle 6:
Invest When Others Can't—Invent the Future**

Our research shows that the Stalwarts kept their feet on the long-term growth accelerator by continuing to spend on R&D. Diamond recently helped a large Property & Casualty insurer manage its innovation portfolio and identify areas to expand the use of technology

to change the nature of relationships with agents and customers. Even in the face of a challenging insurance environment, this innovative insurer is reinventing how agents interact with their customers in a digital world, and investing at a time when its competition is retrenching.

**Principle 7:
Put All Your Eggs in One (or Only a Few) Baskets**

An across-the-board strategy rarely works, whether for cost-cutting or for investment. Scattered diversification increases the chance that the business units with the most potential will be underfunded. Instead of spreading investment across the organization, companies should focus new investment in core strengths or in developing the next core strength. For example, Microsoft invested heavily in one product launch during the '01 recession: the Xbox game console. It was an instant success, selling 1.5 million units in its first two months, making it one of the most successful launches in video game history. A downturn is also a time when firms trim their portfolios of non-core divisions, and double down on the central value of the company. Borden divested its "high-fat holdings" unrelated to the core dairy business in the early '80s recession, and it acquired specific companies directly related to its core business. As a result, the company's average annual net income was significantly higher than that of competitors throughout this period.

What's an Executive to Do?

This is a time when strong leaders can take the initiative to move their companies ahead. Stalwarts and Opportunists increased market value by \$350 billion through the last recession.

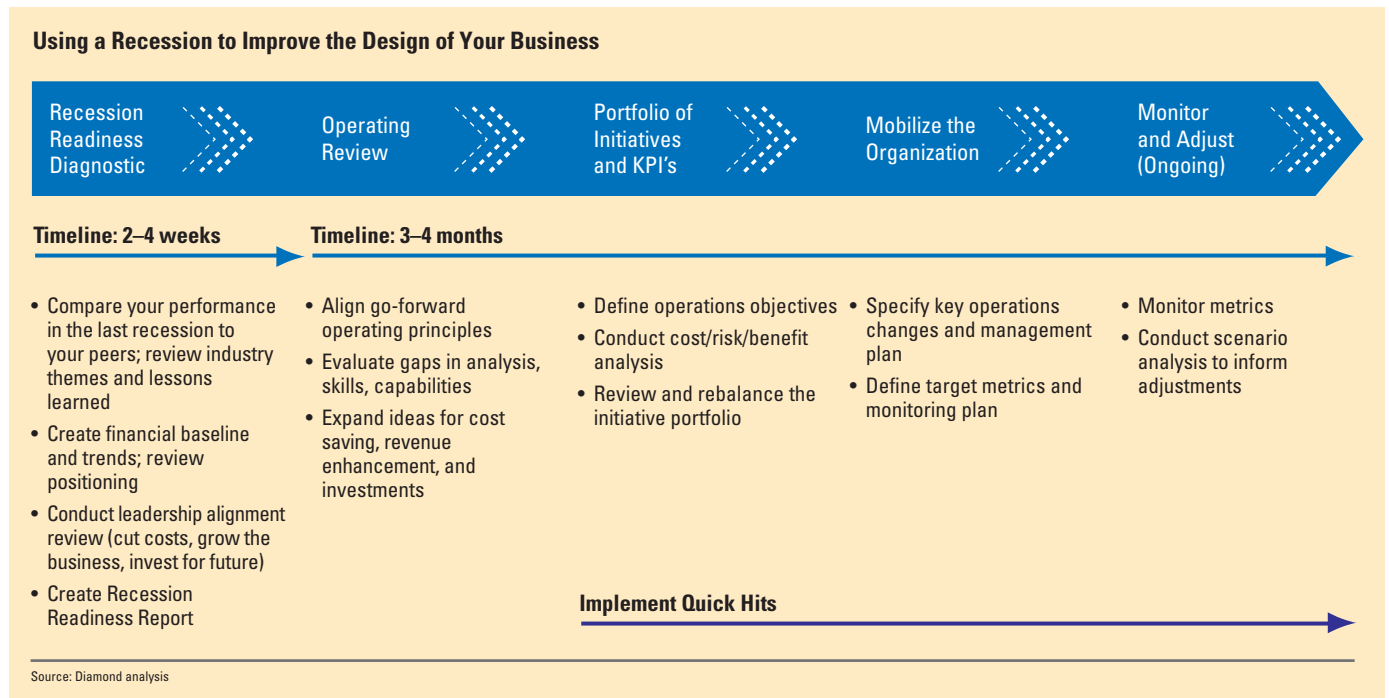


Figure 4

Diamond has worked with companies to analyze quickly where to cut, how to grow, and where to invest to create value following a downturn. Our proprietary approach starts with understanding where your firm stands compared to the market and your competitive set—and determining the “business design” your company needs to win. (see Figure 4, previous page).

Taking action is not without risk. Times of uncertainty can create confusion, cause delay, demoralize organizations, and make staying the course seem like the best option—but staying the course may mean emerging from the recession with a whimper. Leadership that provides an organization with a common set of principles,

uses targeted practices, and carries out a structured plan can proceed through a recession with an Opportunist’s confidence of emerging stronger at the other end. ■

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About Diamond

Diamond (NASDAQ: DTPI) is a management and technology consulting firm. Recognizing that information and technology shape market dynamics, Diamond’s small teams of experts work across functional and organizational boundaries to improve growth and profitability. Since the greatest value in a strategy, and its highest risk, resides in its implementation, Diamond also provides proven execution capabilities. We deliver three critical elements to every project: fact-based objectivity, spirited collaboration, and sustainable results. To learn more visit www.diamondconsultants.com.



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