

What Every Board Director Should Know About Financial Leadership During a Recession

Companies of every size and industry are facing one of the most challenging business environments in history, with unprecedented levels of market volatility, a new administration and staggering declines in consumer confidence and spending. During this critical time, Board Members are faced with extremely difficult decisions that may have long term impact on the organization.

Many of today's issues are driven by complex financial dynamics and Directors without a financial background cannot help but feel heightened personal risk around the choices they are required to make. With shareholder lawsuits in the wings, a Director should consider certain key areas for any organization's financial health.

PLAN, PLAN AGAIN

Here is another area to modify normal processes given the financial landscape. Plan to reforecast quarterly throughout 2009. The November 1st Survey of Business Conditions by executive services firm Tatum found that 30 percent of finance executive planned to create quarterly budgets through 2009. In addition to a quarterly profit plan, create a separate bank budget – and make it very, very conservative. This is different than a quarterly cash forecast—one relates to liquidity while the profit planning re-forecast is used for operational planning purposes and, perhaps, for incentive plan measurements. The risks are great right now and being very thorough in planning will help you minimize surprises.

UNDERSTAND THE CASH SITUATION

Given the credit situation we face, organizations need to focus on managing the funds that are available to make it go as far as is needed. This requires the company to maintain a meaningful 13-week cash flow forecast, tracking and regularly updating the “forecast” to perpetually keep it running one quarter ahead, reflecting new information as it is gleaned. This is not an easy undertaking, but needs to happen quickly because it is the only way to have the visibility to avoid a potentially horrific surprise. Remember the dot-com era when start-ups suddenly realized they couldn't even make a final payroll? A cash-flow forecast is the financial discipline required in today's economy.

One of the most common opportunities to increase cash flow is to improve collections. If the organization has never managed collections diligently, now is the time to see reports on accounts that are past due and to reduce the outstanding balances.

It is also important to recognize that this problem also impacts your key customers. Once a customer gets behind, it becomes difficult to catch up. Reach out early—and often—to have frank conversations with your customers; amend payment terms, reflect current assessments of their credit-worthiness and attempt in all ways to ‘work with them’...but first assure that they are, in fact, a profitable piece of your business and worthy of your flexibility.

The flip side to this coin is managing the timing of payable disbursements – if the organization has historically paid invoices “upon receipt” now is a good time to move to a standard of 30 days.

So what do you do if the company is running low on cash? Many organizations are finding new loans very difficult, so this may be the time to consider selling assets to increase cash flow. Think about which assets are salable without harming operations. If the organization has inventory, managing it closely is critical to avoid tying up cash in inventory that isn't moving. If inventory is not part of the picture, make these decisions carefully – consider bringing in a turnaround or restructuring expert with industry experience as a sounding board, rather than making a decision in haste.

MAKE SURE MANAGEMENT IS SCOURING THE BALANCE SHEET

While it seems obvious to be reviewing the opportunities for efficiencies on the balance sheet, many companies are not in the habit of running the business this way. Directors should be sure to ask questions about potential write-offs or write-downs.

Another major area to consider is financing terms and arrangements. For example, this may be a good time to consider supplier financing if not already utilized. Finance should also be reviewing and renegotiating the financial terms of all large contracts, which can be a relatively easy way to make rapid improvements. If cash flow is an issue management should review all assets to understand what can converted to cash, per the discussion above. If fixed assets are tied to unprofitable businesses, this may be the time to divest of that product line.

FOCUS ON YOUR CORE BUSINESS

Another key to minimizing risk lies in considering whether a business line/product/customer will be viable into the future and focusing on the core. Now is the time to identify the true drivers of profit and accelerate cost containment. An in-depth analysis of every business segment — on a detailed a level as possible – should be undertaken to understand exactly the level of investment or profitability it brings to the overall business. Those that don't measure up — whether products, customers or entire divisions - are candidates for elimination.

If management can't provide reporting on profit by product, business unit, etc., there may be inadequate reporting systems in place. Here again, the need for accurate information is critical, so the effort needs to happen. After all, how can intelligent decisions be made without this insight?

Remember, however, to consider the longer term plan as well. Some business lines may be worthy of management investment and enlightened management will not only analyze assets based on return-on-investment or operating margins, but also the longer term position in a changing market.

In addition to non-core assets, companies must consider core assets producing below average returns, such as a facility that is not profitable or will require a large capital investment. General Electric's decision to sell its appliance unit and Weyerhaeuser's decision to sell its homebuilding business are examples of companies that eliminated assets in the past year as a means to long-term success.

MAKE YOUR WORKFORCE FLEXIBLE

Hiring freezes, layoffs and overall reductions in workforce do not have to stagger businesses. Make your workforce flexible, and use overtime and flexible scheduling options like telecommuting. Remember that staff augmentation can make sense, so erase boundaries and institute a cross functional work force with varying job descriptions. For example, it may make sense to do more audit work internally to reduce fees.

It may also make sense to outsource basic functions and use external advisors to your benefit for tasks that don't require tribal knowledge like general administrative work. Flexible HR management will become a survival skill in the decade to come and considering alternatives now will put you ahead of the curve.

While leading during today's economic downturn presents unique challenges, business leaders must remember that there is life before, during and after periods of distress. It's critical that leaders stay focused on liquidity without losing track of the long term strategy. Remember, investors reward management teams who provide steady, seasoned guidance through emotional times; there is always underlying opportunity to times like these—both personally and professionally.

ABOUT THE AUTHOR

Cynthia Jamison is National Director of CFO Services for Tatum, an Executive Services firm with 37 offices nationwide. She has served as CFO of seven companies and currently chairs the Audit Committees of two publicly traded companies. She can be reached at Cynthia.Jamison@TatumLLC.com

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