

Resource Management: Guidelines For Managing In A Crisis


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ABSTRACT

In times of economic adversity, organizations have multiple courses of action to consider. This paper synthesizes the existing literature from two perspectives – cost cutting and investment for growth. Conditions to consider for each choice are explained, overall recommendations for moving forward are provided, and potential research areas are identified.

Keywords: operations management, cost-cutting, outsourcing, market investment

INTRODUCTION

 Organizations are facing tough times in the current economic environment. Some are struggling for survival; others are trying to capture the opportunity to leverage their processes, technologies, or market positions and to expand where others cannot. While some firms can apply a higher degree of certainty to revenue cycle forecasts, as is the case for those with long-term contractual sales volumes, there is less certainty in firms that are more immediately reactive to their market environment. How do organizations make the tough choices? As this paper will show, the *Business Week* (Nussbaum, 2008) top ten worst things to do in a recession include many things that the organizational literature says work in the long run. How do organizations know when to retrench and when to expand? What has research indicated they should do in the face of downturns? Do they have information to act on, or must they count on ingenuity and luck? This paper explores the research that prescribes two divergent courses of action.

MARKET TURBULENCE

Economic downturns, crises, and recessions – whatever their labels – mean the current economic environment is in turmoil. Market turbulence results in the following predictable characteristics (Goodell and Martin, 1992). Customers change as some gain ground and others go under. Customers and clients plan their expenditures more carefully and with a higher sensitivity to price. At the same time, sweeping price cuts may undercut perceived quality of an organization's products and services. Customers may be looking for lower costs and may be unable to find them within the firm's existing product line. This may cause existing customers to move to a different supplier. However, even during economic challenges, customers are likely to sustain their basic businesses and much of their purchasing will remain consistent to do so.

Market turbulence also results in changes in competitors (Goodell and Martin, 1992). Competitors may react to economic conditions in different ways based on their long-term goals and their power in the market place. If competitors have been through recessions in the past, they have the experience to achieve satisfactory outcomes over time. If competitors are carrying high levels of debt, the current financial situation may put them in a stressful situation. Finally, those firms who have been able to take advantage of economies of scale in the production of their goods and services may drive the competition to a price-only basis to defend or build market share.

All of these are the factors that executives consider when making strategic choices. Each organization needs to consider these factors and their root causes for long-term viability.

SETTING THE STAGE

The first requirement for decision making in a crisis is to determine the objective reality of the organization. Is the organization strengthening its position or is it in immediate trouble? If the latter, a short-term cost-cutting strategy is appropriate. On the other hand, if the organization is fiscally sound, seeking operational efficiency to reduce costs or using marketing tactics to expand revenues may be more suitable strategies. It is more likely that these tactics will have a longer planning horizon, thus providing multiple choices of action; and as such, the resulting or realized improvement timeline is also extended. Organizations can engage in other areas of reform that are synergistic with longer term tactics of investing for growth (Pozen, 2007).

The choice between cutting costs and investing for innovation and growth is significantly driven by the perspective of the executives of the organization (Chattopadhyay et al., 2001). When executives view environmental changes as threats with potential for loss, they pursue internally-focused cost cutting tactics, particularly when the threats are perceived as reducing organizational control over its own performance. Alternatively, viewing environmental changes as opportunities with potential for gain results in investing for innovation and growth. This represents an optimistic view of potential gains from new ideas and technologies. Those organizations that do invest in innovation are more likely to engage in activities that are externally-focused. However, in neither case does the organization differentiate between internally-focused and externally-focused tactics based on whether or not there are slack resources. Instead, such resources are used to undertake the tactics prescribed (Chattopadhyay et al., 2001).

Despite this theoretical framework, organizational literature is not clear on how to differentiate between the two basic tactical decisions of expanding or contracting. If slack resources are not a determinant, then it must be left to organizational understanding and leadership to choose.

CUTTING COSTS

One direction that executives may take to address economic uncertainty is to cut costs. The specific tactics may include downsizing, restructuring, budget slashing, and project cessation. Each may have initial or perceived cost reduction effects. However, these effects may not be sustainable or as realizable as perceived.

One organizational response to crisis is staff downsizing. Though research has demonstrated mixed consequences (McKinley et al., 1995; Mabert and Schmenner, 1997), many organizations look to this tactic to reduce expenses hidden within their processes, both core and ancillary. Staffing and salaries fill a large line in the profit and loss statement and may look ripe for trimming. Yet these are exactly the salaries that represent the core of the business. These are the people who add intrinsic value to the organization. Downsizing may result in hidden costs not recognized in the planning. As reported by Mabert and Schmenner (1997), these costs may include

- Lower quality goods and services
- Increased overtime
- Outsourcing costs
- Lost business opportunities
- Lost productivity

Additionally, downsizing usually results in significantly lower employee morale which may result in the “cesspool syndrome” in which there is significant turnover of highly talented employees and retention of less competent ones (Bedeian and Armenakis, 1998).

Finally, the net benefits that may be realized from downsizing as a cost cutting tactic may not be as immediate or effective as first thought (Mabert and Schmenner, 1998). The benefits from compensation saved must

be reduced by the severance-related costs, the rehiring costs at a later date, and the changes in productivity in the organization. If the cesspool syndrome holds true, those productivity changes may not be linear.

Small and medium sized companies may not undertake full-scale downsizing initiatives, but may reap benefits from some portions of the cost-cutting tactics (DeDee and Vorbies, 1998). Organizational restructuring may be an effective tactic if it provides opportunities for cost containment for customers. Careful management of product development may result in project prioritization that limits the number of projects going on at one time.

Project management overall is an important cost-cutting tactic during economic challenges (Brown, 2008). Viewing the overall portfolio of projects and prioritizing them based on a clear strategy is an important first step. Yet there may be additional projects that need to be included for process optimization and cost reductions. This is also the time that project measurement and event tracking for time and budget performance is even more critical. Though technology can assist, the critical factor is to use a strategic perspective to view projects as means to actualization of the overall strategy. Which projects get the organization closer to their goal, and which ones have a less direct impact? Support the former.

INVESTING AND GROWING

Some organizations view economically challenging times as opportunities to overtake competitors or to open new markets where competition is weak (Srinivasan et al., 2005). Factors that support investment and growth tactics include an existing strategic emphasis on marketing and an entrepreneurial culture. Most of these are not undertaken quickly. A long-term focus that includes progressive and sustained marketing to attain market share is developed with a clear understanding of customer requirements.

Firms that face recession with an existing proactive marketing response achieve better business performance as the recession runs its course. Yet the nature of a proactive marketing plan means that the organizations are not undertaking new or unplanned expenses in marketing. Instead, the marketing plan is already budgeted, so that the organization can reap the benefits without additional expenditures. Proactive marketing plans should allow for flexibility and agility, and the pre-established funds for marketing in such well-positioned companies should not be cut to accommodate budget-cutting needs at a time of crisis.

It is even more important for organizations facing crises to remain strategically flexible (Grewal and Tansuhaj, 2001). This means keeping a good view of the complete organizational environment without focusing on direct competition with others within the industry. A focus on primary markets is an appropriate response to high demand following a crisis or in the face of technological uncertainty (Grewal and Tansuhaj, 2001). However, when facing intense competition, it is better for firms to take a step back and use previously developed strategic capabilities in new ways.

If there is any room for specific talent and skills, challenging times yield some good staffing possibilities. Highly capable people are likely to view uncertainty within their current work situation as an opportunity to move to a firm with more perceived opportunity and stability. This is the flip side of the cesspool syndrome (Bedeian and Armenakis, 1998).

Finally, it is important to consider how organizations view innovation in times of economic downturn. Those organizations that have highly institutionalized missions, diffused power structures, and high levels of resource commitment find it difficult to support innovation and strategic flexibility (Wiseman and Bromiley, 1996; Mone et al., 1998). Those organizations, on the other hand, that can centralize their decision-making power and expand their uncommitted resources can use these resources for just the innovations required to compete favorably even during economic hard times. These innovations have been demonstrated in the form of the first synthetic detergent in 1933 (Dreft) and CNN in 1980 to the iPod in 2001 (Lopez, 2008).

RECOMMENDATIONS

To a large extent, the choices that will be made for each organization come down to two key factors: position and risk. The options available are largely determined by the unique position of the organization within its industry and the time horizon that is central to the decision. The decisions that are made based on these options are a question of balancing risk and reward. Whichever course of action is selected by the firm, there are recommendations to optimize the choice.

1. *Don't panic; plan carefully.* It is important to monitor changes in the economic environment and create either an offensive or defensive strategic posture based on the organization's strengths and weaknesses.
2. *Scan the environment for opportunities before retrenching.* If executive perspective is a determinant in whether an organization focuses on cost cutting measures or growth, it's incumbent upon those executives to at least scan the environment for potential areas of growth before automatically resorting to cost cutting.
3. *Plan proactively to engage in aggressive marketing as part of a strategic focus of the organization.* Such plans may include developing differentiated products, brand recognition, targeted communications, and superior customer service (Srinivasan et al., 2005). Then once these are in place, communicate their strengths within the organization to prevent their becoming targets for cost reduction.
4. *Understand and serve the market at multiple levels through market research.* Ensure a full product line to support those customers who need to move down on the product chain for a time. A broader spectrum of products at different price points allows customers to move to a lower cost product level without the supplier firm cutting prices across the board. This leveraging of product/service diversification to accommodate changing markets highlights the need to identify a firm's best customers.
5. *Identify and focus on your best customers.* With improved measures, specific information on customer transactions can identify those specific customers the firm can grow with. Concentrate on business strategies that meet the needs of the most profitable customers. This may mean not serving other customers as well; but serving the bottom-line enhancing customers provides the greatest overall return to the greatest number of stakeholders (____, 2008). This is especially important if the organization is expanding its product line so customers can move up and down the levels. It is important to identify those customers who are worth that tactic.
6. *Manage the organizational project portfolio carefully.* Project management becomes more important and more intense as economic challenges arise. Developing project management skills and prioritizing the project portfolio will develop organizational strength where it is needed most during crises.
7. *Improve the measurements.* Downsizing firms can undertake measures to keep severance and rehire costs to a minimum while supporting positive productivity gains for improved morale. Central to all cost minimization tactics is better metrics and data tracking of the marginal benefits and costs. When small improvements can account for large cost savings or hidden costs, the identification of the metrics and the comprehensive collection and reporting of those metrics is what determines how the outcomes are perceived (Mabert and Schmenner, 1998).
8. *Identify the root cause of expenses before cutting them.* Again, metrics can help identify what the inherent benefits are of each particular expense (____, 2008).
9. *Don't look to discretionary spending reductions for a major contribution to the bottom line.* As these costs are identified, their importance to the overall strategy may be worth their continuance even though they may appear to be a candidate for cost-cutting.
10. *Always view innovation as an investment rather than a cost.* The only way to keep investment in growth as an option is to continue to pursue innovation in products, services, and processes. When these become viewed as expenses, they become targets for cuts at exactly the wrong time and remove options from the organizational planning portfolio.

CONCLUSIONS

Researching historical precedents and tactical best practices for businesses dealing with tumultuous economic conditions, it is evident that recessions, economic crises, and organizational decline are not new events. They recur with relative frequency, though with different levels of reach and intensity. The current crisis is global in scope and significant in its intensity. It is also publicly reported in the media at a level not previously noted. All of

these factors create a heightened sense of urgency for individuals and organizations. Overreacting or reacting incorrectly to this sense of urgency can be disastrous, perhaps more so than no action at all. This paper has presented two strategic perspectives as revealed in the business literature: cut costs or invest for growth. The recommendations expand the two perspectives into specific considerations, while underscoring the point that these are not mutually exclusive approaches. For many organizations, including those that are tempted to aggressively slash their costs in a time of crisis, the best approach is to pair prudent investment strategies with informed, selective cost-cutting tactics. Above all, leaders and managers alike must respond to the challenges created by the current crisis with action that is thoughtful, deliberate, innovative and yet still consistent with the long-term plans of the business.

FUTURE RESEARCH

The potential exists for further study to expand the contingency model of Mone et al. (1998) that examines an organization's ability to invest and grow during a period of decline. The factors central to this model are included in other literature in the cost-cutting or investing/growing decision-making. Of particular attention are the decision maker moderators that are similar to the executive perspectives of optimism or pessimism that can be found in Chattopadhyay et al. (2001).

Finally, in the costs-cutting literature, there are concerns about the hidden costs or adverse consequences of downsizing (McKinley et al., 1995; Mabert and Schmenner, 1997; Bedeian and Armenakis, 1998). More information about how to cut costs while avoiding the negative side-effects would be useful. Since the economy will continue to rise and fall and since organizations will continue to face these challenging choices, it is important to continue to provide good information about how to make the choices effectively.

AUTHOR INFORMATION

Ellen D. Hoadley, Ph. D., is Professor of Management Information Systems at Loyola College in Maryland where she has taught since 1988. Dr. Hoadley teaches Information Technology and Strategy in the MBA and Executive MBA programs, as well as Systems Analysis and Design at the undergraduate level. Her research areas include business process reengineering, requirements determination in systems analysis, and the use of color in the human/computer interface. Dr. Hoadley has published in journals such as *Communications of the ACM*, *Journal of Business and Economic Perspectives*, and *Journal of Knowledge and Process Management*.

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